

CORPORATE CONTROL AND CONPORTE WRONGDOING:

A CROSS-NATIONAL ANALYSIS OF THE RELATIOSHIP

By

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To the Faculty of Washington State University:

The members of the Committed appointed to examine the Dissertation of  
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Chair

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CORPORATE CONTROL AND CONPORATE WRONGDOING:

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Abstract

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This study examines the relationships between forms of firm controls and corporate wrongdoing, which include tax evasion and bribery, and the moderating effects of national factors, which contain cultural values and social institutions, on the above relationships. Agency theory is used to investigate the relationship between manager-controlled firms and corporate wrongdoing and the relationship between shareholder-controlled firms and organizational deviance. Deterrence theory is used to examine the relationship between family-controlled firms and corporate wrongdoing and the relationship between foreign-controlled firms and organizational deviance. Anomie theory is used to examine the moderating effect of country-level factors.

Two data sets, WBES and PICS, were analyzed using hierarchical linear model. WBES contains 3,731 firms from 29 countries and PICS includes 14,041 companies from 19 nations. Results indicate substantial support for manager-controlled firms, government-controlled firms, family-controlled firms, and foreign-controlled firms. Four cultural variables (i.e., performance orientation, future orientation, in-group collectivism, and power distance) and two social institutions (i.e., the economy and political constraints) show significant moderating effects on different forms of firm control. This research offers insights that are salient to governments and policy-makers to prevent corporate deviance, and to researchers interested in understanding the drivers of firm characteristics and national factors in corporate wrongdoing.

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## DEDICATION

This dissertation is dedicated to my dear parents.

## **Chapter 1. Introduction**

Following the corporate scandals of Enron, Adelphia, and HP, more and more researchers have turned their attention to what factors cause those corporate wrongdoing or organizational deviance. Some even worry that the situation would become a global one in the future. National factors thus become important in this regard. Researchers might have different perspectives toward this issue of organization deviance. In order to have a better understanding of the problem, I plan to investigate the issue through corporate ownership structure and country-level factors. My research questions for this topic are “Do different types of ownership and control have different propensities for firms to be deviant” and “Do cultural values and social institutions influence that relationship?” In other words, the main purpose of the dissertation is to examine the impact of different ownership structures on firm behaviors and how national factors moderate the above associations.

The corporate deviant behaviors discussed in this research include tax evasion and bribery. Slemrod (2004: 878) defines tax evasion as “corporation income tax that legally is owed but is not reported or paid.” I define bribery as an inducement that influences a person to perform his or her responsibilities that are against the individual’s original duties (Pacini, Swingen, and Rogers, 2002). For a company, evading tax could reduce the

tax burden and obtain additional revenues; bribing an official could bring the company additional opportunities, representing potential profits of the firm. However, both behaviors bear the risk of being detected and penalized, which could influence the future possible growth of the company.

To study these two corporate deviant behaviors is important. From a global point of view, they both have negative impacts to the development of a country. Economically speaking, tax evasion could reduce the revenue of the government. The government is therefore unable to make more public investments for economic growth. In order to fill the tax gap, the government might need to increase tax rates, making those who obey the law bear the unfair burden, creating social inequity. As to bribery, it leads the market to operate ineffectively. Bribery would change the established rules of market mechanism. Further, bribery distorts the allocation of the resources in a society. The valuable resources might be used inefficiently, reducing the potential benefits that could have been brought to the community. From the point of view of ethics, tax paying between an individual and the bigger group is a duty (McGee, 2006). Escaping from the responsibility is not ethical. Bribery is not an ethical behavior, either. Ferrell, Fraedrich, and Ferrell, (2002) argue that bribery is an indicator of the standard of ethics in a society. Such behavior would reduce the degree of ethical awareness in the society.

In some research focusing on corporate wrongdoings, several common characteristics are shared. Researchers investigate corporate deviance from the impact of firm level and country level variables. At firm level, variables such as firm size, firm performance, or firm resources are frequently used to predict corporate wrongdoings (e.g., Baucus and Near, 1991). However, very few studies look at the issue from a firm's ownership structure, which is the final decision-making mechanism in a firm. It deserves more attention than it has gained so far. Moreover, few cross-level analyses are available.

Why is cross-level research important? National factors, such as cultures and social institutions, could impact individual behaviors. A national culture is "the collective programming of the mind which distinguishes the member of one human group from another....the interactive aggregate of common characteristics that influences a human group's response to its environment" (Hofstede, 1984: 25). A social institution is a "complex of positions, roles, norms, and values lodged in particular types of social structures and organizing relatively stable patterns of human resources with respect to fundamental problems in life-sustain resources, in reproducing individuals, and in sustaining viable societal structures within a given environment" (Turner, 1997:6). From these definitions, one can understand the potential impact that cultural values and social institutions have on individual firms.

Firm behavior is a product of a complex combination of a firm's inside and outside environment. Previous research usually considers only zero-order effect. Corporate deviance should include "first- and second-order combined effects of variables" (Mckendall and Wagner, 1997: 625). Baucus (1990) argues that company performance cannot be attributed to a single factor. A firm's characteristics, such as strategy, structure, and the environment should be all taken into consideration. To fill the gap, I conduct both zero-order analyses and cross-level studies on organization deviance. There are five different kinds of ownership structures to be discussed in this dissertation, which include manager-controlled firms, shareholder-controlled firms, government-controlled firms, family-controlled firms and foreign-controlled firms. Berly and Means (1932) argue that ownership and control would be separated when a firm grows, but research results (e.g., La Porta, Lopez-de-Silanes, and Shleifer, 1998) show that each firm is usually controlled by a certain unit, such as family or government. Therefore, in this research, I assume that large shareholders of ownership also control the firm, because they could control the decision-makers of the firm through voting. To respond to Baucus' call, I take cultural values and social institutions into consideration regarding their effects on firm deviance. I draw on anomie theory to study whether culture and institutional context give anomic pressures to the relationship between firm ownership structures and corporate

wrongdoing.

In order to increase the validity of the results, I use two different data sets to test several hypotheses. The first data set is the World Business Environment Survey (WBES, 2000) that has 29 nations and 3,731 firms. The countries in the data set range from economically under-developed to developed ones. The second data set is Productivity and the Investment Climate Survey (PICS), which contains 14,041 firms from 19 nations. However, between these two data sets, I expect that PICS contains less variances between countries because the nations in the data set are more homogeneous. They are mostly at the transitional stage and have more similarities among each other. Therefore, the impact from country factors should be less.

The result findings reveal that manager-controlled firms are positively related to tax evasion, that government-controlled firms are negatively related to organizational deviance, that family-controlled firms are positively associated with tax evasion and bribery, and that foreign-controlled firms are negatively related to tax evasion. At the national level, the moderating effects of performance orientation, in-group collectivism, and power distance are found positively significant and the moderating effect of future orientation is found negatively significant. As to social institutions, I do not find that the hypotheses of the moderating effects of polity and economy are supported. The positive

moderating effects of the economy and the negative moderating effect of political constraints are found significant. More detailed explanation of the results is provided in Ch5.



## **Chapter 2. Literature Review**

The literature review section is divided into three parts. The first part is ownership and control; the focus in this section is on the relationships between the five different company controllers and firm performance. The second part focuses on tax evasion. This section reviews the impact of firms' characteristics, cultural values and social institutions on the firms' tax non-compliance. The third part is bribery and corporate wrongdoing. I review the influence of similar predictors on firm behavior as discussed in the second part.

### **Ownership and Control**

#### **Shareholders and Mangers Ownership and Control**

When a company is small, the owner and the controller could be the same person; as the company grows, the shareholders become diversified and the controller might change into professional managers. In their classic work, "The Modern Corporation and Private Property," Berly and Means (1932) argue that modern companies are widely held among small shareholders and controlled by professional managers. The separation of ownership and control brings up agency issues. The agency problems occur because the managers and the shareholders have different goals (Jensen and Meckling, 1976; Ross, 1973). Agency theory proposes that managers are likely to pursue their own interests at the

expense of the owners (Kamin and Ronen, 1978). For instance, managers may purchase other firms to increase their own salaries (Hoskisson and Johnson, 1992) and to reduce their employment risks (Gomez-Mejia, Nunez-Nickle, and Gutierrez, 2001).

That firms are composed of small shareholders causes attention among some researchers. They question the empirical legality of this image. The studies of Eisenberg (1976), Demsetz (1983), and Morck, Shleifer and Vishny (1988) have shown that in the United States, there is some concentration of ownership in big companies. Studies of other developed countries, such as Germany (Gorton and Schmid, 1996), Italy (Barca, 1995), and Japan (Prowse, 1992; Berglof and Perotti, 1994), exhibit more significant concentration of ownership among firms. La Porta, Lopez-de-Silanes, and Shleifer (1998) investigate the final controlling shareholders in twenty-seven rich nations. They conclude that companies are typically controlled by families or governments; the situation is more salient in developing countries than in the developed world. Firms that are held by small shareholder as Berly and Means (1932) describe are not common. Firms in the United States and UK are more diversified because they are controlled by small owners. La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1997) argue that firms in countries with better legal protection for small shareholders are likely to be widely held.

Kaplan and Minton (1994) and Kang and Shivdasani (1995) find that, when firms do

not perform well, Japanese firms with large shareholders are more likely to replace managers than firms without them. Yafeh and Yosha (1996) show that Japanese managers would reduce expenses, such as advertising, and R&D in firms with large shareholders. In the United States, Shivdasani (1993) shows that outside owners with large shares are positively associated with firm takeover. For Germany, Franks and Mayer (1994) find that large shareholders are related to manager turnover. As to firm performance, Demsetz (1983) and Demsetz and Lehn (1985) argue that there should be no association between firm performance and ownership structure, but Shleifer and Summers (1988) present findings of a positive relationship between ownership concentration and firm profitability. Shleifer and Vishny (1997) interpret the conflicting findings as indicating that firm performance might improve at first with larger ownership and the firm performance falls when shares are over concentrated. De Miguel, Pindado, and de la Torre (2004) find that firm value increases at the lower level of ownership concentration due to the monitoring effect and decreases at the higher level of ownership concentration because of the expropriation situation by the large shareholders.

The presence of some significant shareholders might mitigate managers' self-interest behaviors (McConnell and Servaes, 1990; Shleifer and Vishny, 1986). Under the presence of large shareholders, managers may feel obligated to adopt profitable plans or be more

concerned about the owners' welfare. Kroll, Wright, Toombs, and Leavell (1997) argue that in owner-controlled firms, the strategy of acquisition might be due to the potential benefits for the shareholders rather than for the managers themselves. There are some studies showing that shareholder-controlled firms tend to be more profitable than manager-controlled firms. Alcorn (1982) states that companies having owners continuously influencing the operation perform better than other firms. Stano (1976) uses stock market rate of return as measure and finds that firms that are controlled by owners are able to reach significantly higher rates of return than firms that are controlled by managers.

However, there are some alternative views discussed. Levinson (1971) suggests that any business should move from founder-controlled to manager-controlled; it is the "wisest course." From an operation's point of view, many owners react to environmental change slowly (Dyer, 1986), influencing the firm's performance. Flamholtz (1986) argues that firm size is one important factor that directly influences a firm's financial performance. He finds that companies with sales under ten million U.S. dollars have better performance under founder control, while firms with over ten millions U.S. dollars in sales achieve a higher level of performance under manager control. Daily and Daldon (1992) conduct a similar study but do not find any significant differences in terms of

financial performance between manager-controlled firms and founder-controlled firms.

Shleifer and Vishny (1997) also point out that large shareholders might attempt to benefit themselves at the costs of other small shareholders, workers and company managers.

Bergstrom and Kristian (1990) and Barelay and Holderness (1992) do not find such evidence of expropriation by large shareholder in Sweden and in the United States respectively, but Zingales (1994) finds that such problems might be more salient in Italy.

### **Government Ownership and Control**

Compared to private-ownership companies whose first priority is to maximize shareholders' welfare, state-owned companies have different goals. Economists traditionally consider government enterprises the cure of market failure (Atkinson and Stiglitz, 1980). Therefore, government organizations are usually less profit-oriented and more focused on social welfare. Because the whole public shares the operating results of the firms, there is little incentive for government to monitor managers. Many researches have shown that state-owned institutions are less efficient in monitoring performance outcomes related to their investments (Aggarwal and Agmon, 1990; Mehta and Trivedi, 1996; Nebery, 1992).

Officials also use state-owned companies to pursue political goals (Shapiro and Willig, 1990; Shieifer and Vishny, 1994). Boycko, Shelifer, and Vishny (1996) argue that

politicians make government companies hire excessive workers. Krueger (1990) also argues that government firms may be pressured to hire politically influential people who are not qualified to manage the firms. Research in other countries also shows similar results. Davies (1977) examines Australian airline companies and finds that private firms use workers more efficiently and reach better financial performance. In addition, research conducted in Brazil (Harrol, Henriod, and Graziano, 1982), Ivory Coast (Roth, 1984), and Germany (Blankart, 1987) finds that private companies have higher labor productivity in transportation industry or road maintenance services.

Agency theory has been applied to analyze public firms. Cauley and Sandler (2001) treat the manager as the principal and the workers as the agents to explain why organizational change of state-owned firms did not reach the expected results. Andrews and Dowling (1998) use the general public as the principal and the managers of the state-owned enterprises as the agents. They argue that the public has little power or incentive to monitor the managers; thus managers are likely to pursue their own interests at the cost of the firms. As to firm performance comparison, the results are mixed. Vining and Boardman (1992), Boardman and Vining (1989), and Megginson, Nash, and Van Randenborgh (1994) find empirical support that private ownership is more efficient than government ownership. On the other hand, studies from Martin and Parker (1995),

Wortzel and Wortzel (1989), Kay and Thompson (1986) and Caves and Christensen (1980) show that private ownership does not necessarily outperform government ownership. Kole and Mulherin (1997) use U.S. samples from the period after World War II, during which the government had ownership in firms but find no difference in terms of firm performance between private and state-owned companies.

Recently, privatization has been a very popular subject for researchers. By privatizing, private control replaces government control. A lot of studies are conducted in China, as it is the largest centrally planned economic unit. It is generally believed that firms should perform better after privatization. Sun, Tong, and Tong (2002) find no linear relationship between ownership structure and firm performance. They find that firms perform better when firms sell their share in the beginning, but the performance becomes poor when the selling reaches a certain point. However, Dewenter and Malatesta (2001) report that firm performance after privatization have been mixed.

### **Family Ownership and Control**

Evidently speaking, public firms in Asia, Europe, and Latin America are usually family-owned and controlled (Carney and Gedajlovic, 2002; Faccio, Lang, and Young, 2001; Gedajlovic and Shapiro, 1998; Thomsen and Pedersen, 2000). In those firms, family members could also be the CEOs or directors of the firm. Anderson, Mansi, and

Reeb (2003) find that family firms perform better than non-family firms. Also, companies with family CEOs have better accomplishment than companies without them. Villalonga and Amit (2006), using data from Fortune 500, conclude that family ownership increases value when the founder is the CEO.

Demsetz and Kenneth (1985) argue that family concentrated ownership would increase motivation to monitor managers, reducing agency problems, as the family's wealth is aligned with the future of the company. In addition, if the manager needs the firm's technical knowledge, the family is potentially able to offer insightful advice as it has long history in the firm. Stein (1989) suggests that companies that have owners interested in long-period oriented investments are less likely to relinquish potentially profitable investment opportunities. James (1999) suggests that family firms are more efficient in investing than non-family firms because family firms are likely to pass on their business to the next generation. Casson (1999) and Chami (1999) also offer the same argument. Anderson, Mansi, and Reeb (2003) suggest that the long-term presence of family would lower the firm's cost of financial borrowing. When a family member is also the CEO of the firm, "family members have many dimensions of exchange with one another over a long horizon that lead to advantages in monitoring and disciplining" (Fama and Jensen, 1983: 306) the CEO. In addition, there will be more trust among



family members, which would bring together the interests of the managers and the shareholders; the company may thus perform better than firms that do not have family CEOs (Durand and Vargas, 2003; Lee, Lim, and Lim, 2003). From the resource-based view, compared to non-family CEOs, family CEOs have the advantages of accessing special resources, which usually need to be obtained through informal or private channels.

As to the negative impacts of family ownership, DeAngelo and DeAngelo (2000) argue that a family's needs for special dividends are negatively associated with firm performance and the firm's stock price. Shleifer and Summers (1988) note that family owners have the incentive to reallocate rents from workers to the families themselves. From agency theory, family CEOs may conduct strategies that only benefit their families at the cost of other shareholders (McConnell and Servaes, 1990). Furthermore, the relationship between the principal and the agent is based on emotions rather than interests, making the principal-agent relationship more difficult to manage (Schulze, Lubatkin, Dino, and Buchholtz, 2001). Shleifer and Vishny (1997) argue that the biggest cost of having large ownership and control is that the management is still running the company even if they are no longer competent and qualified. Furthermore, using family CEOs could cost the firm the opportunities of hiring more capable managers and talented

executives (Anderson, Mansi, and Reeb, 2003). Schulze, Dino, Lubatkin, and Buchholtz (1999) argue that using family CEOs could bring negative feelings to other senior non-family managers. Although some argue that family ties are unique resources, others respond that such resources are not sufficient enough to be called a competitive advantage, and need to be managed successfully (Sirmon and Hitt, 2003).

### **Foreign Ownership and Control**

Transaction cost theory of Foreign Direct Investment (FDI) offers an explanation of the existence of Multinational Enterprises (MNEs) and their affiliates. Foreign companies must carry some specific advantages, such as managerial expertise and high-tech knowledge, in order to compete in foreign markets where domestic firms have superior knowledge in terms of market situation, culture, and consumer preferences. Caves (1996) argues that companies need to be good at something in order to become multinational. Dimelis and Louri (2002) argue that there should be positive a relationship between foreign ownership and productivity; the transfer of technology that increases along with the amount of ownership should promote output. Griffith (1999) investigates the UK automobile industry and finds that foreign-owned companies are more productive than domestic firms. The main reason for the consequence is in the use of production factors. Foreign companies tend to invest more in physical infrastructures and middle goods.

Globerman, Ries, and Vertinsky (1994) analyze Canadian companies and conclude that MNEs present a higher value-added per worker. Doms and Jensen (1998) examine US companies showing that foreign-established firms have higher total factor productivity than domestically owned firms. Aitken and Harrison (1999) argue that foreign-owned firms may decrease the productivity of local firms because the economy of scale of foreign firms would make domestic companies lose their market share, and the reduction of output is the result. Foreign companies also have a spillover effect on local companies. The situation could happen when foreign companies “lead to productivity or efficiency benefits in the host country’s local firms”(Blomstrom and Kokko, 1998: 249). Dimelis and Louri (2002) find that foreign firms with minority share have the best spillover effect for local firms.

Benfratello and Semenelli (2006) argue that the superior performance of foreign firms might be due to the selection of the industry. MNEs tend to be more concentrated in the industries, such as high tech, and heavily advertised spending business. They also point out that firms’ heterogeneity in terms of age, size, capital intensity and managerial skills might affect firm performance between foreign and domestic firms. Griffith, Redding, and Simpson (2004) find that UK laborers from local firms have lower productivity than laborers from foreign companies, but the differences are bigger in the

manufacturing industry than in the service industry. They also find that foreign enterprises conduct a substantial amount of R&D in the UK. Gomes and Ramaswamy (1999) argue that the costs regarding cooperation and managerial system in foreign markets would increase as the companies go further into culturally different markets. The costs of organizational externalities would cause foreign firms more problems in governance than domestic firms (Buckley, 1997). We thus can understand that foreign firms are not superior in all aspects.

## **Tax Evasion**

### **Firm Characteristics**

Tax revenues from businesses are crucial to the development of a society and its operation of the market economy (Hutton, 2002). Tax evasion from companies would not only make these firms free riders in the economic system, but also unfairly transfer the tax burden to others, such as other businesses or individual households (Christensen and Murphy, 2004). The work of Sutherland (1949) is one of the earliest works to have discussed firm tax evasion. He offers some discussion regarding firm tax evasion without detailed analysis and explanation. However, the study in the area of corporate tax evasion has been scarce so far (Tedds, 2006).

Allingham and Sandmo's (1972) classic model provides the basic framework of

individual tax evasion behavior. In this model, the individual's decision of tax noncompliance is based upon the possibility of being detected and potential punishment. Tedds (2006) suggest that Allingham and Sandmo's model leads to three more propositions, which are that a positive relationship exists between the rate of return for tax evasion and the engagement in the activity; individuals with higher personal income tend to evade tax more, and risk-averse individuals evade tax less. Nearly most economic approaches to tax compliance analysis follow Allingham-Sandmo's framework (Cowell, 1990). This model has expanded into many dimensions during the last three decades (e.g., Border and Sobel, 1987; Cremer, Marchand, and Pestieau, 1990; Mookherjee and P'ng, 1989; Sanchez and Sobel, 1993; Scotchmer, 1987; Trandel and Snow, 1999; Watson, 1985).

Several researchers try to apply the individual-oriented model into business framework. Chen and Chu (2005) argue that business activities are more complicated than those of individuals. As a consequence, the initial model needs to be changed in order to describe business tax compliance. They develop a model in which a firm hires a risk-averse manager who is awarded with forms of compensation as an incentive for tax non-compliance for the firm. Their model implies that a firm would evade tax only when the expected return is considerably greater than expected. Crocker and Slemrod (2005)

propose a model, taking penalties into consideration in their model, which is ignored by Chen and Chu (2005). Crocker and Slemrod (2005) argue that corporate tax evasion would be reduced when penalties are imposed on chief financial officer and that tax evasion would increase if certain adjustment is adopted in the compensation contract.

The forms of firm control and firm size are the main factors to be noticed regarding company tax compliance. The self-employed firms are considered to have relatively higher tax non-compliance because of not having third party reporting (Tedds, 2006). Smith, Pissarides, and Weber (1986), and Pissarides and Weber (1989) use the same data and find that self-employed companies in England underreport their income from 30 percent to 90 percent. Apel (1994) studies the data from 1988 Swedish self-employed firms and finds that the under-reported percentage is 25. Schuetze (2002) studies a longer period of time from 1969 to 1992 and finds that Canadian self-employed companies under-report their revenue by roughly between 11 to 23 percent. Tedds (2005) finds that the differences between the true and the reported income become bigger at the lower-end self-employed income allocation.

Rice (1992), using the data of 1980 IRS Tax Compliance Measurement Program or TCMP, finds that firm size is not positively related to tax compliance. Hanlon, Mills, and Slemrod (2005) are the first to use the data from the Voluntary Compliance Baseline

Measurement (VCBLM) program compiled by the Large and Mid-Sized Business (LMSB) Research Division of the IRS to examine corporate tax non-compliance behavior. They find that the relationship between firm size and tax non-compliance is reflected in a U-shaped form, which means that mid-sized firms have the lowest rate of tax non-compliance, while small and larger sized companies are more likely to evade tax. However, Giles (2000) uses data from New Zealand with a large population of companies, and finds that company tax compliance is positively related to firm size. The results are quite opposite to those of the studies from Rice (1992) and Hanlon, Mills, and Slemrod (2005).

Cloyd, Pratt, and Stock (1996) conducted a mailed survey to public and private firms asking corporate financial executives about their accounting method preferences. They argue that public firms cause a higher cost when they do not fully report their income revenue. There are two main reasons for the argument. First, shareholders tend to use financial methods to evaluate managers' activities; second, the numbers reported in public firms represent market values of the firms, Penno and Simon (1986) agree with the second idea and argue that public firms tend to use income-increasing accounting method than private firms. Hanlon et al. (2005) also find that private firms are more likely to be tax noncompliant. Mills and Newberry (2001) find that, in the earn position, managers in

public firms report higher earnings than private firms; on the other hand, in the loss situation, private firms report less book losses than public firms. Rice (1992) has the similar findings in his study and argues that the reason that public firms have higher tax compliance is that public corporations need to disclose their information of operation to the public. However, Tannernbaum (1993) disagrees with this view and argues that the reason for high tax compliance in public firms is due to the separation of ownership and control.

Tax rates are different among countries; companies might be tempted to transfer their income to regions or nations where lower tax rates are available (Langli and Saudagaran, 2004). Some European countries reduced their corporate tax rate between 1984 and 1986; while the United States followed in their footsteps between 1986 and 1988. Klassen, Lang, and Wolfson (1993) analyze 191 American multi-national firms in response to worldwide tax rate changes during the period of 1984 to 1990. They differentiate between U.S. and non-U.S. firms and suggest that firms respond to tax rate changes in predictable ways. Harris, Morck, Selmrod, and Yeung (1993) examine 95 American international firms from 1984 to 1988 and find that firms that have lower tax liability have legal presence in nations with low tax rates. Hariss (1993) and Jacob (1996) suggest that multi-national corporations shift income to reduce tax costs. Grubert,



Goodspeed, and Swenson (1993), and Grubert (1997) found that foreign-controlled firms have lower tax liabilities than U.S.-owned firms, as they might transfer their income to other countries; the research of Collins, Kemsley, and Shackelford (1997) has similar results. Interestingly, Grubert and Mutti (1991) and Hines and Rice (1994) use national level data and examine the influence of corporate tax rate. They find that the foreign branches of American multi-national companies report higher profits in countries with low tax-jurisdictions.

### **Culture Values**

In the cross-cultural research of tax evasion or tax compliance, the focus is not on the comparison of using Hofstede's cultural dimensions or other similar contexts; authors emphasize the comparison of national differences in terms of social norms and how these social norms influence tax compliance. Alm and Martinez-Vazquez (2001) divide social norms into internal and external categories. Internal social norms refers to "how the taxpayer judges his or her own compliance behavior in light of the individual's own feelings about what is proper acceptable or moral behavior" (Alm and Martinez-Vazquez, 2001: 10). The internal social norm is positively related to tax morale (Torgler, 2004), meaning intrinsic motivation to pay taxes (Frey, 1997). External social norm is concerned with "how the taxpayer feels he or she is treated by government in such areas as the

payment of taxes, the receipt of government services, or the responsiveness of government decisions” (Alm and Martinez-Vazquez, 2001; 10).

Alm et al. (1995) conduct the same tax compliance experiment in both the United States and Spain, countries with different cultures but similar tax systems. The researchers find people from America consistently show higher tax morale than people in Spain. They ascribe the differences to the factor that the U.S. has higher social norms in terms of tax compliance. Alm and Torgler (2006) use data from World Value Survey examining tax morale and find that America has higher tax morale than fifteen other European countries. They argue that tax morale is influenced by the relationship between taxpayers and the government, and personal characteristics. They suggest that democracy, trust in government, and the degree of religious belief are positively associated with tax morale. Pommerhne and Weck-Hannemann (1996) find that tax evasion is negatively associated with political control. Torgler (2003) finds that a stronger democratic system leads to better tax compliance. Studies of Alm et al. (1999) and Feld and Tyran (2002) both show that more group decision-making on tax issues would reduce tax evasion.

Torgler (2004) studies Costa Rica and Switzerland and finds that Costa Rica has higher tax morale. In more general findings, the study proves that both internal social norms and external social norms are associated with tax morale and tax compliance.

Cummings, Martinez-Vazquez, McKee, and Torgler (2004) use data from the United States, South Africa, and Botswana to examine whether cultural differences predict tax compliance. They conclude that different tax compliance among countries can be explained by the perceptions of equity of governmental administration, the perceived fairness of fiscal exchange, and overall attitude toward respective governments.

Interestingly enough, Brandts, Saijo, and Schram (2004) investigate four nations including Japan, the Netherlands, Spain, and the U.S. and conduct an experiment on voluntary contribution to public goods, but find no cultural differences among these countries. They argue that behavioral differences are minor across cultures when the game or the rules are similar, implying that if tax systems are similar among countries, there should be no differences in terms of tax compliance or tax evasion.

### **Social Institutions**

Some researchers argue that social norms would influence tax behaviors (e.g., Elster, 1989). Fehr and Gächter (1998: 854) define a social norm as “behavioral regularity that is based on a socially shared belief how one ought to behave which triggers the enforcement of the prescribed behavior by informal social sanctions.” Although the majority of the research focuses on the individual tax decisions, CFOs or CEOs are thus influenced by those factors regarding their tax decision-making, and further their companies’ tax

policies are impacted. Putnam (1993) states the importance of social capital in the governance of a society; some authors point out that trust is a key feature in maintaining social operation of production (Gambetta, 1988; Hardin, 1993). Slemrod (1998) argues that voluntarily willing to pay taxes would reduce the cost of the governmental operation. There are some studies (e.g., Alm, Sanchez, and De Juan, 1995) focusing on different countries with similar fiscal systems, but different tax compliances. The main findings from these researches are that people who comply with taxes might view tax evasion as immoral and societies with greater social cohesion have higher compliance.

Communication among groups in a society is also important to tax behavior. Alm, McClelland and Schulze (1999) argue that the social norms of tax compliance could be influenced by group communication. They find that individuals change their level of enforcement after communicating with others. Bohnet and Frey (1994) suggest that communication would transfer a group decision into an individual one, which means that the behavior of tax compliance is mutually influenced. Kidder and McEwen (1989) argue that the more people who are involved in setting up rules, the more likely that people will comply with that rule, meaning that if the tax rule is agreed to by the majority of the people, the situation of tax evasion could be decreased.

The relationship between ethnic fractionalization and tax compliance has caused

much attention recently. Some experiments from different areas such as social psychology and political psychology have found that the degree of trust and the level of trustworthiness is negatively associated with ethnic diversity (Alesina and La Ferrara, 2002; Glaeser, Laibson, Scheinkman, and Soutter, 2000; Tyler, 1998; Zucker, 1986); they also find that trust and tax compliance are positively related (Scholz 1998; Scholz and Lubell, 1998a,b; Scholz and Pinney, 1995). The very basic argument here is that people are willing to be tax compliant if they know other people will be the same. Laseen (2007) argues that the ethnic fractionalization would decrease the level of trust in the bigger group, and thus would increase the reluctance to contribute to the other ethnic groups.

The extent to which taxpayers feel satisfaction with their government seems to be crucial. Taxpayers are more compliant with taxes if public services offered by the government are equitable with the paid tax. Several studies (e.g., Spicer and Becker, 1980; Spicer and Lundstedt, 1976; Song and Yarbrough, 1978) base their research on the equity theory, viewing the government and the taxpayers as an exchange relationship. Tyler and Smith (1998) explain that the equity theory is important because it proposes that the objective outcomes would influence people's feelings and behaviors. They argue that the lack of equity between taxpayers and the government would create distress, and tax evasion could be the result. Alm, Jackson and McKee (1992) conduct an experiment in

which public goods are offered and find that tax compliance is always higher when public goods are shown, indicating that if the government could provide companies with more services or build more public infrastructure that benefit the community, the whole community and the firms will be less likely to evade tax.

The effects of audits on tax compliance causes attention among researchers. Murphy (2003) suggests that how tax authority treats taxpayers and whether taxpayers feel that the authority trusts them are crucial in determining taxpayers' behaviors. Beron, Tauchen, and Witte (1992) study the influence of audits on income reports and reports of subtractions on the tax returns. They use data including reported Adjusted Gross Income (AGI) and reported tax liabilities. They find that the increase of an audit significantly influences reported AGI and tax liabilities among certain income level groups. Tauchen, Witte, Beron (1989) divide income groups into four different levels, and investigate the effect of audits on reported income. Their findings suggest that audits would stimulate all groups to report higher income, meaning that more governmental inspection will force more honest income reports, but only the highest income group shows statistically significant results. Erard (1992) examines whether subjects would be more tax compliant in the following year after experiencing many audit evaluations, but finds no conclusive results. The author also compares those who experienced an audit in the previous year

with those who did not experience such treatment, and still finds no significant different results in terms of tax behaviors in the following year. However, Ratto, Thomas and Ulph (2005) suggest that if tax compliance were considered a social norm in the community, tax audit would be more effective than if tax compliance was not related to social norm.

## **Bribery and Wrongdoing**

### **Firm Characteristics**

There has been little research focusing on the relationship between ownership structure and firm illegal behaviors. McKendall, Sanchez, and Sicilian (1999) propose that a positive relationship exists between the proportion of inside directors to outside directors and the number of environmental violations, that if the CEO is also the chair of the board the likelihood for the firm to violate environmental regulation will increase, and that the stock value owned by directors and managers will increase environmental violations. However, only the third hypothesis is found statistically significant. In Kesner, Victor, and Lamont's (1988) study, they propose that the portion of outside directors to its board should be negatively related to the illegal behaviors of a firm and that outside-director dominating board should commit fewer illegal behaviors than inside-director dominating board. However, neither of the above hypotheses is found significant.

Many research have examined the relationship between organization size and firm wrongdoings. However, earlier studies (e.g., Clinard, Yeager, Brissette, Petrashek, and Harries, 1979; Conklin, 1977) do not find support for the association. Not long after, Simpson (1986) finds that large firms are more likely to be illegal. Yeager (1986) points out that large organizations are associated with more wrongdoings based on two reasons. The first is that these large companies are more able to absorb penalty from the government. Second, when organizations become bigger, the increasing number of divisions may facilitate the repression of stigma that exists in the complex corporation. Finney and Lesieur (1982) argue that the communication and coordination among units become difficult when an organization becomes larger and thus problems, violations or even wrongdoings could occur. Baucus (1994) argues that when firms become larger and more complex, they might engage in pursuing growth strategies and innovative strategies, which could lead to illegal results. Vanghan (1983) states that the larger size of firms increases their complexity, which can create problems for communicating and control, resulting in illegal behaviors. Further, big firms have multiple branches and thus might have more illegal activities, since the members in the organization become less visible. Baucus and Near (1991) categorize firms into large, median, and small. They find that large firms are twice as likely to be illegal than small ones, while median firms are about



10 percent higher. Although Lane (1953) finds positive association between firm size and wrongdoings, the samples in the study are from one specific industry rather than generalized.

As firms increase in their size, they need to decentralize and empower, thus creating more chances for illegal activities within these firms (Vaughan, 1982). Hill, Kelly, Agle, Hitt, and Hoskisson (1992) follow Yeager (1986), and argue that large firms would commit more violations in absolute number and thus might have proportionally more wrongdoings per unit than small firms. Studies by Asch and Seneca (1976), Baucus and Near (1991) and Perez (1978) all suggest positive association between firm size and firm wrongdoing. These studies do not calculate the proportional part. The research by Clinard et al. (1979) and Clinard and Yeager (1980) find that large firms commit more violations than smaller ones, but the results are reversed if the calculation uses proportion. Yeager (1986) concludes that the above situation is due to the fact that the big companies are able to offer more expensive equipments that help the firm obey the regulation.

Some studies (e.g., Hay and Kelly, 1974) argue that bigger firms do not commit more wrongdoing, but attract more attention for investigation due to their size. Mckendall and Wagner (1997) argue that large size firms are more visible and their activities may be more likely to be detected. However, Dalton and Kenser (1988) have an opposite view

that large firms can influence the regulation and thus are more likely to abide the law.

Some negative association between firm size and wrongdoing is also found or suggested.

In Cohen's (1992) study, those companies that violate environmental regulations are smaller ones. Companies under the investigation of Security and Exchange Commission in Shapiro's (1984) study are smaller in terms of size. Further, Joyce (1989) argues that smaller firms are more likely to engage in antitrust violation than large firms. Martin et al. (2006) argue that small firms have an increased rate of engaging in wrongdoing and their survival depends on outside resources (Svensson, 2003). Therefore, small firms are more likely to engage in illegal behavior, such as bribery.

Structural complexity is also associated with corporate wrongdoing (Donaldson, 1982). Structural complexity refers to the combined effects of horizontal, vertical, and spatial differentiation. Vertical differentiation is associated with supervision; horizontal differentiation is concerned with interdependent tasks; and spatial differentiation refers to the distribution of organization operation. Structural complexity is related to communication, coordination, and managerial control issues. When an organization increases its complexity, the flow of information can be impeded. Managers at the top might not be able to receive correct information (Jackall, 1988; Stone, 1975), which may result in than making wrong decisions in violation of rules. Some studies find positive

relationships between organizational complexity and organizational wrongdoings (e.g., Herling, 1962; Ungar, 1972; Vandivier, 1972). Decentralization refers to the locus and dispersion of decision making in an organization. Several researchers (e.g., Chandler, 1962; Child, 1984; Williamson, 1975) argue that large sized firms and diversified firms would create pressure for their operation to be decentralized, letting more people make decisions freely. This situation could cause more wrongdoing to the companies.

Sonnenfeld and Lawrence (1978) conclude from their case study research that in decentralized organizations, illegal acts are more likely to be committed.

Corporate strategy is also considered to potentially impact the firm's behavior.

Dabout et al. (1995) argue that diversification, especially unrelated diversification, might influence a firm's behavior in two ways. First, the head office would evaluate divisional performance based on financial criteria; the leaders of those division offices might reduce expense at the cost of violating regulations. Second, a diversified firm might contain the stigma that could potentially influence the whole group. Hayes and Abernathy (1980) argue that in diversified firms, top management are likely to judge those sub-units by numbers. As a result, divisional managers would likely emphasize short-term performance rather than long term, and potential wrongdoing could be the outcome.

When accomplishing the goal is stressed, managers are more inclined to focus on the

short-term goal in order to obtain desired results (Hoskisson and Hitt, 1988).

With the increasing globalization, the level of corruption of local governments also influences firms' foreign entry policy. Uhlenbruck, Rodriguez, Doh, and Eden (2006) investigate 220 telecommunications companies in 64 emerging economies, and find that firms facing corruption often times choose entry mode with nonequity. Voyer and Beamish (2004) examine the relationship between corruption and Japanese firms' foreign investment policy. The results suggest that high corruption, which happens more in developing economies that have weaker regulation, has a negative impact on the firms' investments.

The motive for a firm to engage in illegal activities has been attributed to the concerns about the firm's profitability, which is considered one of the most influential factors for firm behaviors (Clinard and Yeager, 1980; Gross, 1978). Low financial performance can press firms to engage in deviant behaviors (McCaghy, 1976). Martin et al. (2006) argue that firms facing financial troubles might engage in deviant behaviors to create opportunities for themselves. Significant negative relationships between firm performance and corporate wrongdoing is found in some research (e.g., Staw and Sz wajkowski, 1975). During the period that a company is having poor financial performance, they may attempt to cut cost in order to save expense, sometimes even

violating regulations (Daboub, Rasheed, Priem, and Gary, 1995). In the study of Clinard and Yeager (1980), they find that firms among Fortune 500 that have poor financial performance tend to violate regulation more than those firms with good performance. In the studies of Baucus (1988) and Baucus and Near (1991), no statistically significant results are found in the association between firm performance and wrongdoing.

Organizational culture is another important issue related to organizational wrongdoing.

Several researchers argued that an organization's climate could either encourage or discourage illegal activity in the organization (Victor and Cullen, 1988). Kulik (2005) argues that Enron's collapse is mainly due to its agency-theory oriented corporate culture in the company. McKendall and Wagner (1997) suggest that strong ethical climate in an organization could reduce the association between organizational factors and its wrongdoings.

### **Cultural Values**

Culture plays an important role in the business environment, because it could influence both individual and organizational behavior within its context. Whether people or organizations decide to engage in corruption is heavily associated with cultural values. Some cultures indeed lead people to pay less attention on avoiding deviant behaviors (Tanzi, 1994). Previously, most cross-cultural studies are based on Hofstede's (1997)

dimensions. Power distance means “the extent to which the less powerful members of institutions and organizations within a country expect and accept that power is distributed unequally” (Hofstede, 1997:28). Cohen, Pant, and Sharp (1996) argue that people from high power-distance value would be more likely to accept unethical behaviors than people from low power-distance value.

People from individualism culture are more self-centered and care about their own welfare (Parboteeah, Parboteeah, Cullen, and Basu, 2005). In contrast to individualism, people from collectivism view themselves as part of a bigger group in exchange for loyalty. Although some researchers (e.g., Viteil, Nwacukwu, and Barnes, 1993) argue that individualism is more associated with corruption; others have the opposite view (Banfield, 1958; Hooper, 1996). The main argument is that, in contrast to individualism, collectivism focuses on creating long lasting relationships, which could lead to deviant transactions, such as bribery. Cullen et al. (2004) find that this cultural value would significantly reduce managers’ unethical thinking, which is the opposite of their original hypothesis.

The cultural dimension of masculinity-femininity is related to “material success” rather than “quality of life” (Hofstede, 1997: 82). This cultural dimension is strongly achievement-oriented. It focuses on the acquisition of money and power. It views the

pursuing of the high accomplishment as an ideal. Getz and Volkema (2001) argued that, under the value, the end is more important than the means; people could pursue their goal through informal channels, such as bribes. The relationship between the cultural value and corruption in their study is nearly significant. Martin et al. (2006) propose that the cultural value of achievement is positively associated with firm bribery. However, the result does not support their hypothesis.

Hofstede (1997: 113) defines uncertainty avoidance as “the extent to which members of a culture feel threatened by uncertainty or unknown situations.” People seek to be in stable conditions, including norms, regulations and rules. Where the outcomes are uncertain, corruption could be viewed as a way to reduce that uncertainty. Rashid (1981) argues that bribery is able to reduce uncertainty in contracting in the third-world countries. Getz and Volkeman (2001) argue that companies that have corrupted would continue to do so in order not to break the rules. In their study, they not only find a main effect between the cultural value and corruption; further, they hypothesize that uncertainty avoidance would moderate the relationship between economic adversity and corruption, and the finding is supported.

## **Social Institutions**

When the public sector and private sector interact with each other, corruption might happen. Bribery is likely to occur when governmental officials have the right to distribute resources (Rose-Ackerman, 1994). Private sector bribes in order to get benefits and avoid costs. What might be potential factors that influence the behavior of bribery? From an institution's point of view, the punishment for the corruption, and the governmental structure to allocate resources could influence such behavior. These issues could be examined from two dimensions, the accountability of politics, which is associated with democracy, and the governmental structure to deliver public goods, which is associated with centralization or decentralization of the government organization.

A large amount of literature has discussed the influence of political accountability on corruption (e.g., Djankov, McLiesh, Nenova, and Shleifer, 2001; Fackler, and Lin, 1995; Nas, Price, and Weber, 1986; Laffont and Meleu, 2001; Persson, Roland, and Tabelini, 1997). Generally speaking, the democratic system is negatively related to corruption. In Treisman's (2000) study, the researcher concludes that countries that have been a democracy consistently since 1950 are inclined to have low corruption. Lederman, Loayza, and Soares (2001) point out that political competition, which means election, would reward those who perform well and control politicians' behaviors, because such a



system could reduce prejudiced politicians (Bailey and Valenzuela, 1997; Linz and Stepan, 1996; Rose-Ackerman, 1999) and decrease corruption. Furthermore, the election system could reduce the political stability by changing the ruling party. Political stability might be positively associated with corruption as strong relationships between certain government officials, the resource distributors, and private sectors could be established and last, certain interest groups might always benefit from the relationship. Thus, Triesman (2000) argues that there should be negative association between political instability and corruption; as the system could guarantee that national policies could benefit the country as a whole rather than certain interest groups.

However, Henisz (2004) argues that democracy might not guarantee that policies made would benefit the nation as a whole. An executive with over all control with legislative and executive power could still bring severe corruption. Therefore, some researchers turn their attention to the examination of political constraints positioned on the discretion of policy-makers (e.g., Clague, Keefer, Knack, and Olson, 1996; Durham, 1999; Knack and Keefer, 1995). Henisz (2004) argues that political structures that put checks and balances on decision-makers could not only stabilize the legal and political environment, but also reduce short-term political policies or incentives that only benefit certain groups where corruption might happen. Martin et al. (2006) use this concept in

their study and argue that political constraints on government leaders could reduce the bribery activities from firms.

In the studies of the association between economics and corruption, there are two different focuses. Some scholars are concerned about how economy influences corruption while others care about whether corruption has positive or negative impact on economic performance. Economists have treated economic development as a crucial factor for corruption (Macrae, 1982). Nearly every study uses Gross Domestic Product (GDP) per capital to predict corruption on a national level. The general conclusion is that high GDP per capital is associated with lower corruption (Wu, 2005). Gets and Volkema (2001) find that under the situations of economic hardship, which means less resources are available, both individuals and organizations are more likely to engage in unethical behaviors in the market (Beeman and Sharkey, 1987). The availability of resources in the market thus becomes a very important indicator for corruption. Wu (2005) finds that the openness of a country to foreign competitors could reduce corruption. Treisman (2000) points out that the increasing competition would limit the ability of governmental officials to protect bribe payers. Thus, businessmen might not have to bribe in exchange for special favors, because even doing so, the future for their success will still be highly uncertain.

In the meantime, discussions about the relationship between corruption and

economy are mixed. Leff (1964), Huntington (1968) and Brunetti (1995) are of some scholars who hold relatively positive opinions about corruption. From a global point of view, Leff (1964) first argued that the government might not be aware of the future development of economic activities. Through bribery, businessmen can be more effectively engaged in developing economy. Second, the bureaucratic system intervenes in the economy to an extensive degree. Bribery can shorten the process and mobilize the movement of the whole bureaucratic process. Third, investors face three different aspects of uncertainty: the demand side of the market, the supply side of the market, and the influence of the government. Bribery can reduce the uncertainty from the governmental side. However, Getz and Volkema (2001) argue that bribery has a high opportunity cost. First, if the money paid is not in productive use, the resource is thus wasted. Second, the most efficient firm might not be chosen. Further, such action increases the risks for potential punishment for the company in the future.

Education is a crucial social institution. Jones, Thomas, Agle, and Ehreth (1990) suggest that educational level is positively associated with moral development. Rest and Thoma (1986) find that the development of moral judgment is influenced by education. Williams, Barrett, and Brabston (2000) argue that business education might create more business wrongdoings and suggest that managers with a MBA would strengthen the

association between firm size and the firm's illegal activities; the similar suggestion could be also found by Daboub et al. (1995). Cullen et al. (2004) find that the more accessible education is in a country, the lower the level that managers in the country would justify their wrongdoing, suggesting positive influence of education on organizational deviance.

In summary, the brief overview of extant research shows that corporate wrongdoing is the result of different factors and is a fairly complicated situation. There is hardly any consistent conclusion we could draw from previous studies, which means that there are still a lot un-discovered parts in this area to be examined. Firm behaviors are not the consequence of collection of zero-order analysis (McKendall and Wagner, 1997) but the results of a combination of environmental factors and firm characteristics (Baucus, 1994). The present study therefore fills in the gap by examining corporate wrongdoings from firm-level variables as well as national-level factors.

### **Chapter 3. Hypothesis Development**

In this chapter, I develop hypotheses to be tested and explain anomie theory that serves the theoretical rationale for the moderating effect in the study. In the first part of the chapter, I discuss the hypothesis development regarding the associations between ownership structures and corporate wrongdoings. In the second part, I introduce the rationale and the application of anomie theory. In the third part, I explain the selection of cultural variables and social institutions as moderators. The last part in this chapter is the hypothesis development of the moderating effects.

#### **Ownership Structures and Corporate Wrongdoings**

In this part, I discuss the relationships between five different forms of corporate controls and firm deviant behaviors. For manager-controlled firms and shareholder-controlled firms, I argue that manager-controlled firms are more likely to engage in bribery and tax evasion, while shareholder-controlled firms are less likely to engage in organizational deviance. My argument is based on agency theory (Jensen and Meckling, 1976; Ross, 1973). The theory argues that managers are risk-averse and self-interest oriented. Because the agent (managers) and the principal (shareholders) have different goals, managers are likely to pursue their own interests at the companies' or shareholders' costs. The main goal of managers is to maximize their own interests while

the goal of shareholders is to maximize the company's profits.

Tax evasion and bribery could indeed bring profits for a company in the short term. Evading tax could reduce the company's expense and increase its total revenue. Further, the saved money could be used for future investment, attracting potential investors. As to bribery, it could make the firm win over competitors when they compete with other firms for the same plans. Bribery could stimulate business development and circumvent regulations, saving time that could otherwise be wasted due to the bureaucratic system. Moreover, bribery can establish relationships with officials, reducing uncertainty for business operation and offering more opportunities for the firm in the future. However, bribing and evading tax could put the company in a dangerous position. First, tax evasion and bribery are illegal. Governmental institutions might be able to detect such behaviors. Second, the company is facing potential penalty if it conducts such behaviors. The money fined would influence its daily operation and cost its future investment opportunities. Moreover, conducting tax evasion and bribery might jeopardize the company's goodwill, which is difficult to estimate financially and hard to rebuild.

Managers face income risk, employment risk, and reputation risk. They need to have good performance evaluation in order to reduce those risks. Bribery and tax evasion could bring short-term interests for them and thus reduce the risks they are facing. For

instance, evading tax could instantly increase the total profits of a firm, making the manager's performance evaluation more competitive. Therefore, managers have a stronger motive to engage in these behaviors. As to shareholders, although the company could enjoy the short-term benefits, in the long run, the company might face stronger threats, such as penalty. The shareholders' interests would be seriously hurt, if the company engaged in such behaviors. As a consequence, there is little incentive for shareholders to bribe or to evade tax.

Bribery is considered the supply side of corruption, which is usually defined as the abuse of official roles and resources for private interest (Goudie and Stasavage, 1997; Klitgarrd, 1995; Rose-Ackerman, 1978; Spinellis, 1996; Tanzi, 1994). The government usually plays the role as the bribe receiver rather than the supplier. If a government-owned company needs to obtain extra information or to stimulate the development process, it can appeal to other governmental institutions rather than bribe. Bribing thus does not seem to be an option for a government-controlled company to engage in. As to tax evasion, there is less motivation for a government-controlled firm to evade tax, either. Government-owned companies are usually not profit oriented but social welfare oriented. The decision-makers in these organizations are not appointed based on their abilities, but on political reasons. Therefore, these decision-makers would not be

evaluated according to the company performance; hence, evading tax in order to achieve a better financial outcome for the firm and running the risks of engaging in illegal behaviors becomes unnecessary.

As to family-controlled firms and foreign-controlled firms, I draw on an influential social control theory, deterrence theory, to argue that family-controlled firms are more likely to engage in deviant behaviors while foreign-controlled firms are less likely to engage in corporate wrongdoings. Deterrence theory assumes that individuals would calculate the costs and the benefits before taking an action (Varma and Doob, 1998). People would be more inclined to commit a crime if the benefits outweigh the potential costs (Andenaes, 1974; Cornish & Clarke, 1986). On the other hand, an increase in the perceived costliness would discourage people from committing it (Gibbs, 1975; Zimring and Hawkings, 1973). The costs taken into account include the possibility of being detected and the potential punishment. Between the two factors, some findings suggest that the potential punishment is not as important as the possibility of being apprehended (Varma and Doob, 1998). There has been a long-standing belief that the theory is “especially useful in understanding corporate crime” (Paternoster and Simpson, 1996:550).

Family-controlled companies have been described as having unique intangible



resources. Family members emphasize family values more than corporate values. They are known for their commitment and honesty to the relationships (Lyman, 1991). Trust among family members is another salient and important characteristic in family-controlled firms. With trust among one another, people are more likely to have consensus in decision-making. From the perspective of deterrence theory, the solid interpersonal relationships and strong group agreement in family-controlled firms would make it less likely to reveal to the people outside the group the important information circulating around the group, which, I argue, would reduce the chance of being apprehended when family-controlled companies engage in bribery or tax evasion. Furthermore, family-controlled businesses tend not to have many codes of ethics (Adams, Taschian, and Shore, 1996). Researchers suggest that the lack of control would lead to a higher propensity to commit crimes, because people would be less influenced by sanctions threats (Nagin and Paternoster, 1994; Nagin and Pogarsky, 2001; Piquero and Tibbts, 1996). The situation would also increase the possibility for family firms to be deviant.

There are many ways for a multinational company to operate in a foreign country. The firm can either cooperate with local firms or operate the business independently. The advantages of cooperating with other firms include gaining broader knowledge about

local customer preferences, governmental regulations and rules, and cultural differences.

More important, the local firms might be able to introduce useful local connections to the foreign firm. On the other hand, the disadvantages of the business mode are that the multinational firm needs to share its advanced technologies and managerial experiences with the local firms, creating potential competitors once the relationship terminates.

When a foreign firm runs business more independently, it would have fewer opportunities to learn more knowledge about local regulations and to obtain helpful connections. From the perspective of deterrence theory, I argue that foreign-controlled firms are thus less likely to engage in deviant behaviors, such as bribery and tax evasion, because they have higher opportunities to be detected. Bribery is related to governmental officials; companies need to have special connections to conduct the deal. And, evading tax requires specific knowledge in regards to tax laws. Without having accesses to governmental officials and sufficient knowledge about tax regulations, engaging in those behaviors becomes dangerous and risky. Therefore, the chance for foreign-controlled firms to be deviant decreases.

Based on the above arguments, the following hypotheses are proposed.

*Hypothesis 1a: There is a positive relationship between manager-controlled firms and tax evasion.*

*Hypothesis 1b: There is a positive relationship between manager-controlled firms and bribery.*

*Hypothesis 2a: There is a negative relationship between shareholder-controlled firms and tax evasion.*

*Hypothesis 2b: There is a negative relationship between shareholder-controlled firms and bribery.*

*Hypothesis 3a: There is a negative relationship between government-controlled firms and tax evasion.*

*Hypothesis 3b: There is a negative relationship between government-controlled firms and bribery.*

*Hypothesis 4a: There is a positive relationship between family-controlled firms and tax evasion.*

*Hypothesis 4b: There is a positive relationship between family-controlled firms and bribery.*

*Hypothesis 5a: There is a negative relationship between foreign-controlled firms and tax evasion.*

*Hypothesis 5b: There is a negative relationship between foreign-controlled firms and bribery.*

## **The Development and Application of Anomie Theory**

In this section, I discuss the theoretical background and the application of anomie theory. The word “anomie” is from Greek word *anomia*, meaning normlessness or “without law” (Oru, 1987). It refers to social instability that results from the breakdown in generally accepted values and individuals’ feeling of uncertainty. Durkheim introduces the concept of anomie in 1893 in his renowned book, *The Division of Labor in Society*. In the book, Durkheim describes anomie as the unfair division of labor within the society; the inequity of division of labor causes the breakdown of regulation and the results are conflicts among classes, because people no longer know what the expectations are.

Durkheim argues that normlessness leads to deviant behaviors. In his other classic work in 1897, *Suicide: A Study in Sociology*, he views anomie as the result of sudden economic and social change of modernization that causes a weakening of traditional social controls that are based on social relationships and family structures, and the result of anomie is the increased rates of deviance.

Robert Merton borrows Durkheim’s idea of anomie, but does not agree with him. Merton argues that anomie is not the result of sudden social change. He defines anomie as “a condition of normlessness and social disequilibrium where the rules once governing conduct have lost their savor and force” (1964:226). In addition, Merton also takes social

structure into consideration and argues that when a social structure is unable to offer enough opportunities to everyone to reach the socially desired goals, the social system would press certain classes of people to select deviant means to reach socially desired ends. Therefore, anomie is a social-structural condition, rather than a reflection of individual characteristics (Menard, 1995).

For Merton (1938), the main purpose of anomie theory is to discover “How some social structures exert a definite pressure upon certain persons in the society to engage in nonconformist rather than conformist conduct...high crime rates of deviant behavior in these groups [occur] not because of the human beings comprising them are compounded of distinctive biological tendencies but because they are responding normally to the social situation in which they find themselves.”

For Merton, among the components of cultural and social structure, two are specifically important. The first is culturally desired goals and interests. It serves as the basic purpose for people in the society to accomplish. The second important factor is the socially agreed upon regulations that control the means to reach those goals. However, it should be noted that these two factors operate jointly not in a predictable way. The interaction might result in a situation that stresses the value of specific goals, while giving little concern to the suitable modes to reach the ends. Under this context, Deflem

(1989) argues that anomie is believed to refer to a general imbalance between culturally desired goals and the legitimate methods to achieve those accomplishments.

Researchers divide Merton's theory into two theories, anomie theory (macro-level) and strain theory (micro-level). Anomie theory focuses on the relationship between cultural values and legitimate means to reach those values. The theory explains the variation in crime rates across societies. At macro-level or strain theory, Merton considers how individuals adjust to the patterns of means and goals. Merton uses American society as an example. He argues that American society focuses on monetary reward (i.e., the "American Dream"). However, not everyone has access to obtain legitimate means to achieve, causing some people to reject legal means. According to Merton, the allocation of using illegal means is not random; the class structure functions in such a way that "The greatest pressures towards deviation are exerted upon the lower strata" (Merton, 1968:198). People from lower social classes who do not have access to reach legitimate means of accomplishment are more likely to engage in deviant behaviors. Therefore, "It is the combination of the cultural emphasis and the social structure which produces intense pressure for deviation" (Merton, 1968:199).

Merton does not assume that everyone would accept the same goals and means in a society. There are five modes of adaptation to social goals and means. Conformists accept

both the goals and the means to reach them. Innovation means that people accept social goals but have few legal means to reach the goals; they design their own methods.

Ritualists give up the goals but obey the rules. Retreatists reject both the means and the goals. Rebels reject the cultural goals and legal means, but create their own goals and means.

Messner and Rosenfeld (1994) follow Merton's anomie theory and develop an institutional anomie theory (IAT). In Merton's concept, emphasizing the cultural goals would give anomic pressure to individuals; institutional anomie theory expands the concept to include the effect of social institutions, such as family, education, and political system on individuals' behaviors. There are two key concerns in institutional anomie theory. The first is that the level of crime depends on the interrelated dynamics between cultural values and social institutions. The second is that the situation conducive most to high rates of crime is when capitalist cultures dominate the balance of power over social institutions. Capitalist cultures may press for economic success at the cost of social institutions. Therefore, non-economic mechanism becomes unattractive, weakening social controls. In this theory, there are four distinct market-oriented cultural values. Achievement refers to the use of material means to evaluate one's success. Individualism involves the concept of personal competition in order to reach material success.

Universalism is concerned with the idea that the chance to succeed is open to everyone.

Pecuniary materialism focuses on promoting the value of money, which is dependent of other kinds of material rewards.

Anomie theory is originally developed from sociology. It has been used in explaining cross-national crime and social condition. For instance, Messner and Rosenfeld (1997) examine how homicide rates in different countries are influenced by political restraint posted on economy. Kim and Pridemore (2005) investigate social change, institutional anomie, and criminal behavior in Russia. In recent years, anomie theory has been applied to the area of management. Cullen, Parboteeah, and Hoegl (2004) are the first to introduce institutional anomie theory in cross-national management. They investigate the relationships between cultural values and social institutions and managers' ethical reasoning. They suggest that when discussing the expectation of managers' behavior, their social background should be taken into consideration, which is Merton's concept. Johnson and Cullen (2005) extend the original concept of anomie theory and propose a new theory called institutional anomie theory of entrepreneurship. They argue that entrepreneurial activities can be understood as positive deviance. When there is an imbalance between cultural values and legitimate means, individuals could resort to creating their own ways, which are not necessarily against the laws or regulations, to



reach the socially desired goals. Martin, Cullen, Johnson, and Partoteeah (2006) apply the concept of anomie theory and locate their focus on firm behavior, rather than individual behavior. They examine the relationships between firm characteristics, national cultures and social institutions and firm-level bribery. Their samples contain over 4,000 firms from 39 countries.

### **National Factors and Corporate Controls**

There are four cultural values and three social institutions to be examined as moderators in the study. Cultural variables include performance orientation, future orientation, in-group collectivism, and power distance; social institutions include the polity and economy, the economy, and political constraints.

Based on agency theory that is related to performance evaluation and time preferences, I thus use the culture values of performance orientation and future orientation to test their moderating effects on manager-controlled firms and shareholder-controlled firms. As to government-controlled firms and family-controlled firms, the two types of organizations are all associated with groups and the distribution of power or bureaucracy inside the institutions. Therefore, the cultural factors of in-group collectivism and power distance are used to test their influences. I do not use any cultural variable to test its influence on foreign-controlled firms. Based on the definition of

culture, which is “the collective programming of the mind which distinguishes the member of one human group from another....the interactive aggregate of common characteristics that influences a human group’s response to its environment” (Hofstede, 1984: 25), foreigners are not likely to hold the same values as local people do and cultural values do not impact foreigners as much as expected, making it less sensible to test.

As for social institutions, three variables are associated with resource allocation or resource control in a society. They are likely to influence firm behaviors. Therefore, all forms of corporate controls, except for government-controlled firms, are tested with three social institution variables. However, I only investigate the influence of the economy on governmental-controlled firms. The variable of the economy refers to industrialization and capitalism, in which the government does not heavily influence the society. Consequently, governmental-controlled firms would not be in a conflicting role as the judge-and-player at the same time. I list the relationships discussed above in Table 1.

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Insert Table 1 about here

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## **The Hypothesis Development of Moderating Effects**

### **Cultural Values**

**Performance Orientation** Performance orientation “reflects the extent to which a community encourages and rewards innovation, high standards and performance improvement” (House et al., 2004:239). The cultural value of performance orientation suggests that a society that emphasizes performance orientation values individuals who are able to perform and who are able to generate results (Tromenaars, 1994). The cultural dimension is built on Weber’s work and McClelland’s concept of achievement. In his famous book, *The Protestant Ethic and the Spirit of Capitalism* (1904 [1930], 1904 [1998]), Weber analyzes the differences between Catholic and Protestant religions. He finds that the fundamental difference between these two religions is their attitudes toward work. Weber argues that Catholics focus on “good works” in order to fulfill religious purposes. Good works include praying, confessing, and donating, which are distinct from daily activities. In other words, earthly work has nothing to do with religious purpose. On the other hand, the Protestant combines the meaning of work and religious belief. Hard work becomes a way to reach religious purposes. In other word, the religion encourages people to work so that they can reach the end of the religion. With his colleagues, McClelland (1955, 1958, 1961) introduces the concept of a need for achievement. It is

defined as “the need to do better all the time” (McClelland, 1987:228). McClelland argues that people with a high need for achievement are inclined to work on tasks whose future successes are not guaranteed and to collect information to improve their work performance.

In a community that emphasizes performance, rewards are offered to individuals or firms for accomplishment; performance appraisals are used to evaluate results, and there is “a sense of urgency” (House et al. 2004). Meanwhile, Trompenaars and Hampden-Turner (1998) categorize ascription-oriented culture and achievement-oriented culture as two opposing values in a country. In ascription-oriented culture, people are evaluated based on their social status, which might include age, gender, social connections, and educational background (Trompenaars and Hampden-Turner, 1998). As to achievement-oriented value, people are judged based on what they have reached. Cullen et al. (2004) argue that the more a society focuses on achievement-oriented value, the more likely that the community would give less concern to means used to reach these outcomes. The result, from the perspective of anomie theory, is the increase of deviance for individuals or decision-makers of firms. The deviant behaviors of tax evasion and bribery become more likely to occur.

Moreover, in corporations, decision-makers’ performance is usually evaluated based

on financial reports. A better financial statement for a firm could not only reflect higher capabilities of the company's controllers but also reduce the employment risk of the firm-controllers. However, those financial statements are often reported to the public periodically, or are rather short-term oriented. The time pressure would also push decision-makers of a firm to engage in wrongdoings, such as tax evasion and bribery, in order to reach a better outcome in the short-term. Thus,

*Hypothesis 6a: The positive relationship between manager-controlled firms and tax evasion is enhanced with greater performance orientation in a country.*

*Hypothesis 6b: The positive relationship between manager-controlled firms and bribery is enhanced with greater performance orientation in a country.*

*Hypothesis 7a: The negative relationship between shareholder-controlled firms and tax evasion is reduced with greater performance orientation in a country.*

*Hypothesis 7b: The negative relationship between shareholder-controlled firms and bribery is reduced with greater performance orientation in a country.*

**Future Orientation** As a cultural dimension, future orientation is considered a basic value in all communities (Kluckhohn and Strodtbeck, 1961), and is related to time orientation (Trommsdorff, 1983). It is defined as “the extent to which members of a society or an organization believe that their current actions will influence their future,

focus on investment in their future, believe that they will have a future that matters, believe in planning for developing their future, and look far into the future for assessing the effects of their current actions” (House et al., 2004: 285), indicating that people in a society with high future orientation would evaluate the future consequences before they make their decisions. These people are not attracted by short-term gains at the cost of long-term goals.

This cultural dimension of future orientation is related to Hofstede’s (2001) culture value of Confucian dynamism, which measures the degree to which a society focuses on values that look toward the future. The long-term orientation contains values including hard work, patience, thrift, etc. It is argued that individuals living under high Confucian dynamism dimension consider using shortcuts to reach short-term benefits more negatively than individuals under low Confucian dynamism dimension (Cohen, Pant, and Sharp, 1996).

Some research has related future orientation to individual deviant behaviors. Keough, Zimbardo, and Boyd (1999) have found that people who are more future-oriented are less likely to engage in drug, tobacco, and alcohol use. Meanwhile, people with strong future orientation are able to control themselves from involvement in tempting behaviors. They would consider future influences more before engaging in these behaviors. Also, Hirsch,

Duberstein, Conner, Heisel, Beckman, Franus, and Conwell (2006) find that people with higher future orientation tend to have less suicide ideation. They argue that, future orientation involves the ability to consider the potential results.

From the perspective of anomie theory, I argue that individuals or companies under low future orientation culture are more likely to engage in deviant behaviors. Under this context, in order to obtain short-term benefits, they are more inclined to resort to quick ways, such as tax evasion and bribery, to reach their ends. As to people or firms under high future orientation value, they are less likely to engage in aberration behaviors.

Although bribery or tax evasion could bring benefits to an organization in the short-term, in the long run, the firm might face penalty or the loss of goodwill of the company; they would carefully consider the negative consequences before engaging in those behaviors.

Moreover, Swaidan, and Hayes (2005) propose that people with long-term orientation are more sensitive to ethical issues than people with short-term orientation. As we have discussed previously, tax evasion and bribery are all ethically suspect behaviors.

For decision-makers under future orientation value, they would consider the moral aspects of engaging in such behaviors and thus are less likely to be deviant. As to

decision-makers under low future orientation culture, ethics are not a major concern.

Therefore, engaging in tax evasion and bribery is a possible selection for them to reach

their goals. Therefore:

*Hypothesis 8a: The positive relationship between manager-controlled firms and tax evasion is reduced with greater cultural value of future orientation in a country.*

*Hypothesis 8b: The positive relationship between manager-controlled firms and bribery is reduced with greater cultural value of future orientation in a country.*

*Hypothesis 9a: The negative relationship between shareholder-controlled firms and tax evasion is enhanced with greater cultural value of future orientation in a country.*

*Hypothesis 9b: The negative relationship between shareholder-controlled firms and bribery is enhanced with greater cultural value of future orientation in a country.*

**In-group Collectivism** The cultural value of collectivism has been used broadly to differentiate between cultures (Kluckhohn and Strodtbeck, 1961; Sondergaard, 1994) and applied in different subjects (Hofstede, 2001; Segall and Kagitcibasi, 1997; Triandis, 1995; Trompenaars, 1994). This cultural value is compared to individualism in regards to the relationship between the individual and the group. Hofstede (1980:51) defines both cultural dimensions as “individualism pertains to societies in which the ties between individuals are loose; everyone is expected to look after himself or herself and is his or her immediate family. Collectivism as its opposite pertains to societies in which people



from birth onwards are integrated into strong, cohesive in-groups, which throughout people's lifetime continue to protect them in exchange for unquestioning loyalty." Thus, in collectivism culture, people depend on groups and view group goals as more important than individual accomplishment, while in individualism culture people tend to be more self-interest oriented. In Hofstede's (1984) study, he finds that countries in North American and Western Europe are more individualistic, and nations in Asia, African, and Latin America are collectivistic.

In the GLOBE study (House et al., 2004), the researchers measure collectivism construct at both organizational and societal levels. At national level, or under institutional collectivism, people are more likely to join group activities and emphasize relatedness with different groups. At organizational level, or under in-group collectivism, people tend to view themselves as highly interdependent with the organization and are willing to sacrifice themselves for the goals of the organization. The major difference between institutional collectivism and in-group collectivism is that, under in-group collectivism, people's social relationships are more limited and constrained; they focus on their closest circles, such as family and work place.

Wood, Longenecker, Moore, and Carlos (1988) find that the value of collectivism strongly influences individuals' ethical reasoning and hence their behaviors. Collectivism

emphasizes the relationships among people and individuals acknowledge the obligations and responsibilities toward other members in the same cultural community. People would consider the consequences of their behaviors toward others before taking actions.

Therefore, high institutional collectivism value is expected to reduce deviance inside the country. However, at organizational level or in-group collectivism, people's care and concern are within their limited circles. They pay less attention to people outside the circle who may even share the same national cultural values. As a result, the impact of their behaviors to others outside their circles is beyond their consideration. Hence, engaging in wrongdoings, such as tax evasion and bribery, are more likely to happen.

Further, under high in-group collectivism, individuals' survival depends on the survival of their organizations. The goals of the organizations become the goals of the individuals. In order to survive, the individuals must strive to meet the organizational goals. From anomie theory's perspective, the emphasis on the organizational goals would give individuals or decision-makers anomic pressure and decrease their care about the methods selected to obtain the goals. In other words, in order to accomplish the organizational goals, engagement in aberration behaviors, such as tax evasion and bribery, is more likely to occur.

*Hypothesis 10a: The negative relationship between government-controlled firms and*

*tax evasion is reduced with greater cultural value of in-group collectivism in a country.*

*Hypothesis 10b: The negative relationship between government-controlled firms and bribery is reduced with greater cultural value of in-group collectivism in a country.*

*Hypothesis 11a: The positive relationship between family-controlled firms and tax evasion is enhanced with greater cultural value of in-group collectivism in a country.*

*Hypothesis 11b: The positive relationship between family-controlled firms and bribery is enhanced with greater cultural value of in-group collectivism in a country.*

**Power Distance** The cultural dimension of power distance is defined “as the extent to which the members of institutions and organizations within a country expect and accept that power is distributed unequally” (Hofstede, 1997:28). It is a “measure of the interpersonal power or influence between B and S as perceived by the least powerful of the two, S” (Hofstede, 1984:71), S representing subordinate and B for boss. Power distance influences organizations in different aspects, such as organizational structure, decision-making mechanisms, and the degree of career satisfaction. For example, organizations in high level of power distance culture tend to be hierarchical; the subordinates are expected to follow the instructions from their bosses without questions;

and the workers have lower career satisfaction. On the other hand, firms in low level of power distance have more flat structures; there is less distance between the managers and the non-managers; employees have higher career satisfaction.

I expect that firms in high power distance culture are more likely to engage in bribery and tax evasion than firms in low power distance culture. People under high power distance put emphasize on authority; they are less likely to question the deviant behaviors of their bosses. The implication is that decision-makers have more tolerance for deviance, which could lead to anomic conditions. They would have less doubt about engaging in bribery or tax evasion because they are less sensitive about ethical issues (Swaidan et al., 2005). In contrast, individuals in low power distance culture are more likely to question moral issues. Research has found that managers in low power distance countries tend to view questionable behaviors as unethical (Christie, Kwon, Stoeberl, and Baumhart, 2003), suggesting that they have less tolerance for deviant behaviors, such as bribery and tax evasion.

Basing on equity theory (Adams, 1965), Parboteeah et al. (2005:128) argue that people would compare themselves to others and attempt to reduce inequity. Individuals might engage in “self serving” behaviors in order to decrease the level of inequity. As such, this cultural dimension is related positively to people’s willingness to justify

ethically suspect behaviors, suggesting that this cultural value stimulates aberration behaviors. I apply their argument to the firm level. For firms, not every company has the same status in terms of financial condition or future prospect. For instance, some firms have a better financial performance than other companies. For these firms, their financial condition is able to attract more potential investors. Further, these firms are also capable of investing in promising projects, creating opportunities for their future. On the other hand, those companies with low financial performance are less likely to gain attention from investors and are unable to participate in rewarding plans. For these companies, engaging in deviant behaviors, such as bribery and tax evasion, could assist them to obtain a better financial position or gain better investing opportunities. In other words, the cultural dimension of power distance would give firms anomic pressure in order to pursue a more competitive position.

*Hypothesis 12a: The negative relationship between government-controlled firms and tax evasion is reduced with greater cultural value of power distance in a country.*

*Hypothesis 12b: The negative relationship between government-controlled firms and bribery is reduced with greater cultural value of power distance in a country.*

*Hypothesis 13a: The positive relationship between family-controlled firms and tax evasion is enhanced with greater cultural value of power distance in a country.*

*Hypothesis 13b: The positive relationship between family-controlled firms and bribery is enhanced with greater cultural value of power distance in a country.*

## **Social Institutions**

**The Polity and Economy** Polity is “the consolidation and concentration of power or the capacity to control and regulate others for the purpose of mobilizing, allocating, and distributing a population and its resources towards ends and goals (Turner, 1997:58). In other words, the polity or the political institution may serve to help reach the collective goals (Messner and Rosenfeld, 2001). Meanwhile, Olsen (1991:215) defines economy as an “interrelated network or system of beliefs (concerning work, property, construct, and wealth), activities (extraction, production, and distribution), organizations (business firms, labor unions, consumer associations, regulatory agencies), and relationships (ownership, management, employment, sales) that provide the goods and services consumed by the members of a society.” Economy is an important institution in all societies.

The state plays two important roles as economic coordination and the appropriation and redistribution of economic wealth (Knusten, 1995; Turner, 1997) in the economy.

The state could be either active or passive in the intervention of economic activities.

More active involvement of the state represents a more socialist economics system, ranging from the centralized planning of communist systems to redistributive welfare of

the Western social democracies (Esping-Anderson, 1990). Less active involvement of the government in the economy represents a capitalist-oriented society where control over “major economic resources is delegated, albeit to varying degree, to private owners and their agents (Whitley, 1994:154).

Some studies have focused on the relationship between economic factors and deviant behaviors. In Gartner’s (1990) study, the researcher finds that economic inequality positively relates to crime behaviors, suggesting that the lack of economic resources stimulates individuals to engage in wrongdoing. Fiala and LaFree (1988) find that low level of welfare spending partially contributes to child abuse. Messner and Rosenfeld (1997) find that the degree of decomodification (the degree to which the state’s policies protect the individuals from the impact of market force) is negatively related to homicide rates. Savolainen (2000) finds that social welfare policies interact with other culture drivers and have a significant impact in reducing deviant behaviors. Also, Pratt and Godsey (2002) suggest that social support has a negative association with the rate of violent crime, consistent with the prediction of anomie theory that high social support would reduce the temptation for people to be deviant.

From the perspective of anomie theory, a more welfare-oriented or redistributing economic system would inhibit individuals or firms from involvement in deviant

behaviors. Governments with more socialists systems provide people with expansive redistributive benefits such as health care, welfare programs, housing, etc. (Rossides, 1990). When people or firms receive resources and services from the economic system, the logic of anomie theory promotes the conclusion that there is less need for individuals or companies to use illegitimate means to obtain resources in order to reach their goals. In other words, in high social welfare-oriented society, it is less likely that bribery and tax evasion by firms would occur.

*Hypothesis 14a: The positive relationship between manager-controlled firms and tax evasion is reduced with greater level of welfare socialism in a country.*

*Hypothesis 14b: The positive relationship between manager-controlled firms and bribery is reduced with greater level of welfare socialism in a country.*

*Hypothesis 15a: The negative relationship between shareholder-controlled firms and tax evasion is enhanced with greater level of welfare socialism in a country.*

*Hypothesis 15b: The negative relationship between shareholder-controlled firms and bribery is enhanced with greater level of welfare socialism in a country.*

*Hypothesis 16a: The positive relationship between family-controlled firms and tax evasion is reduced with greater level of welfare socialism in a country.*

*Hypothesis 16b: The positive relationship between family-controlled firms and*



*bribery is reduced with greater level of welfare socialism in a country.*

*Hypothesis 17a: The negative relationship between foreign-controlled firms and tax evasion is enhanced with greater level of welfare socialism in a country.*

*Hypothesis 17b: The negative relationship between foreign-controlled firms and bribery is enhanced with greater level of welfare socialism in a country.*

**The Economy** In contrast to a welfare-oriented system, in the less redistributive political system, control over economic resources resides, in varying degree, with private owners and/or their agents (Whitley, 1994:154). The capitalist system is a more “self-serving economic system where everyone looks out for his/her own interests” (Ralston, Holt, Terpstra, and Kai-Cheng, 1997). The basic logic behind the capitalist system is that the market would provide necessary distinct rewards to individuals for their efforts. However, people under this society lack the extensive safety nets. Individuals need to work for their survival without the protection from the government. According to anomie theory, the self-interest oriented system would increase anomic pressure for firms and individuals. Moreover, when individual economic roles dominate other roles, such as family membership, the traditional social controls are undermined. The situation would also lead to the increase of anomie, which in turn would promote deviant behaviors. In other words, economic domination damages traditional social ties found in

more mechanistic societies (Durkheim, 1893), leaving members in the societies facing conditions that encourage the pursuit of egoistic goals. Firms under this context, in order to survive, are more likely to ignore the consequences of using illegal means. As a result, engagement in corporate wrongdoings, such as tax evasion and bribery, are more likely to occur.

*Hypothesis 18a: The positive relationship between manager-controlled firms and tax evasion is enhanced with greater level of economic dominance in a country.*

*Hypothesis 18b: The positive relationship between manager-controlled firms and bribery is enhanced with greater level of economic dominance in a country.*

*Hypothesis 19a: The negative relationship between shareholder-controlled firms and tax evasion is reduced with greater level of economic dominance in a country.*

*Hypothesis 19b: The negative relationship between shareholder-controlled firms and bribery is reduced with greater level of economic dominance in a country.*

*Hypothesis 20a: The negative relationship between government-controlled firms and tax evasion is reduced with greater level of economic dominance in a country.*

*Hypothesis 20b: The negative relationship between government-controlled firms and bribery is reduced with greater level of economic dominance in a country.*

*Hypothesis 21a: The positive relationship between family-controlled firms and tax*

*evasion is enhanced with greater level of economic dominance in a country.*

*Hypothesis 21b: The positive relationship between family-controlled firms and bribery is enhanced with greater level of economic dominance in a country.*

*Hypothesis 22a: The negative relationship between foreign-controlled firms and tax evasion is reduced with greater level of economic dominance in a country.*

*Hypothesis 22b: The negative relationship between foreign-controlled firms and bribery is reduced with greater level of economic dominance in a country.*

**Political Constraints** North and Weingast (1989) argue that political institutions characterized by checks and balances can have positive effects on investment. The government is able to credibly commit not to engage in policy change with respect to investments and to increase accountability and transparency (Lee, 2005). In contrast, Henisz (2000) argues that frequent and potential arbitrary changes in taxation, regulatory or other relevant economic policies increase investment uncertainty

Political systems with fewer checks and balances would suggest an unstable environment for businesses to operate. Policy makers are able to change regulations to satisfy their needs. Given that the investments from firms are irreversible, a government has an incentive to change tax or other rules with the knowledge that investors do not easily to withdraw those investments. In order to deal with the situation, firms might need

to be deviant in order to maintain their competing position. Hence, corruption or tax evasion is likely to occur under these conditions. A system of checks and balances in the political institution stabilizes and legitimizes the political environment in a country (Henisz, 2004), reducing the chance for government to be corrupted and the potential anomic pressure for firms to engage in bribery and tax evasion.

On the other hand, countries with high levels of political constraints provide more credible and legitimate institutional environments that discourage deviant behaviors and corruption among governmental officials and decision-makers of firms. Further, high political constraints offer a stable environment that attracts private investment. For instance, in the study of Stasavage (2002), the researcher finds that countries moving from an authoritarian system to a political system where different parties control executive power and legislative power would be positively related to private investment. Thus, political structures that impose checks and balances on policy-makers minimize the possibility for politicians to respond to short-term policy change (Henisz, 2004) and maintain the stability of the environment. Thus,

*Hypothesis 23a: The positive relationship between manager-controlled firms and tax evasion is reduced with greater level of political constraints in a country.*

*Hypothesis 23b: The positive relationship between manager-controlled firms and*

*bribery is reduced with greater level of political constraints in a country.*

*Hypothesis 24a: The negative relationship between shareholder-controlled firms and tax evasion is enhanced with greater level of political constraints in a country.*

*Hypothesis 24b: The negative relationship between shareholder-controlled firms and bribery is enhanced with greater level of political constraints in a country.*

*Hypothesis 25a: The positive relationship between family-controlled firms and tax evasion is reduced with greater level of political constraints in a country.*

*Hypothesis 25b: The positive relationship between family-controlled firms and bribery is reduced with greater level of political constraints in a country.*

*Hypothesis 26a: The negative relationship between foreign-controlled firms and tax evasion is enhanced with greater level of political constraints in a country.*

*Hypothesis 26b: The negative relationship between foreign-controlled firms and bribery is enhanced with greater level of political constraints in a country.*

## **Chapter 4. Research Methodology**

The main purpose of the dissertation is to examine the associations between corporate structures and corporate wrongdoings and how cultural values and social institutions moderate those associations. In order to increase the validity of the test, I conducted two studies, using two different data sets to test the hypotheses. Each of the data set contains different numbers of countries but has the same dependent variables, which are bribery and tax evasion. This chapter is organized as follows. First, I discuss the two different studies and their data characteristics. Next, I introduce the dependent variables, independent variables, moderators, control variables, and the analytical tool.

### **Two Studies**

**Study One** The data used in study one is the World Business Environment Survey (WBES, 2000). This comprehensive project conducted by the World Bank Group and partner institutions involved firms in 80 nations across the globe. World Bank researchers located in different nations conducted personal interviews. The content of the survey is translated into different languages to ensure its consistency. The main questions in the survey include regulations, economic policies, corporate governance, and infrastructure and financial barriers.

From the World Bank sample of 80 countries, appropriate data are available for 29

countries. The total sample size is reduced due to the availability of cultural values, social institution values, and the dependent variables. However, there is no alpha value for either dependent variable because they are composed of only one single item respectively.

The 29 countries are Argentina, Brazil, Canada, Colombia, Costa Rica, Ecuador, El Salvador, France, Georgia, Germany, Guatemala, Hungary, Indonesia, Italy, Kazakhstan, Malaysia, Mexico, Philippines, Poland, Portugal, Russia, Singapore, Slovenia, Spain, Sweden, Turkey, United Kingdom, United States and Venezuela.

In total, there are 3,731 firms in study one. As to firm size, 82% of the samples are small and medium companies (those with 500 or fewer workers). With regards to industry, 31% of the companies are from manufacturing industry, 56% are from the service industry, and the rest are in agriculture industry and others. The average age of these firms when the data was collected is 23 years old. The number of firms in each country is listed in Table 2.

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Insert Table 2 about here

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**Study Two** The data set used in study two is the Productivity and the Investment Climate Survey (PICS). The surveys are aimed at obtaining information for official

evaluation of investment climate from an international and regional perspective. The World Bank Group has supported several surveys conducted in regions including North and Sub-Saharan Africa, South Asia, East Asia, and Latin America. It mainly focuses on developing economies. The surveys share the purpose of generating data needed for profiling the investment climate of an economic unit in comparison with the international and regional business environment, and the goals of policy reform as well as policy research.

The original data set in PICS is fairly complex and contains more than 50,000 companies in more than 50 nations. The whole data set is composed of the work done by the World Bank's newly established Investment Climate Unit and other data sets such as the Firm Analysis and Competitiveness Surveys (FACS) of the World Bank's Development Economics Group and the Regional Program for Enterprise Development (RPED). I remove the countries for which I am unable to find cultural values, indexes for social institutions, and firms without the report of ownership structure or the status of bribery and tax evasion. As a result, there are 19 nations and 14,041 firms in the final data set. The 19 countries include Albania, Egypt, El Salvador, Georgia, Germany, Greece, Hungary, Indonesia, Ireland, Kazakhstan, Korea, Philippines, Poland, Portugal, Russia, Slovenia, South Africa, Spain, and Turkey.



As to the characteristics of the firms in the data set of PICS, 48.9% of the companies have the number of workers below 20; 28.9% of the firms have workers ranging from the total number of over 20 to below 100. In regards to the industry, almost 49% of the firms belong to the industry of manufactory. The number of companies in each country is listed in Table 3.

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Insert Table 3 about here

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### **Dependent Variables**

The dependent variable in the dissertation is corporate wrongdoing, which includes tax evasion and bribery. Slemrod (2004: 878) defines tax evasion as “corporation income tax that legally is owned but is not reported or paid,” and bribery is an inducement that influences a person to perform his or her responsibilities that are against the individual’s original duties (Pacini, Swingen, and Rogers, 2002). However, there is no validity value reported for either of the variables, because the measure of both tax evasion and bribery is composed of only one item. In the data set of WBES, the selection of the degree of wrongdoings is based on scales. In PICS, participants needed to fill in the blank with the actual number of those activities. Detailed information of the original questions in both

data sets is listed in Appendix A.

### **Independent Variables**

The independent variable in the study is corporate control or corporate structure, which refers to the decision-makers of a firm. The final decision-makers of a firm could be different individuals or a group, such as managers, shareholders, bank, etc. Different decision-makers might have distinct thinking processes, which lead to diversified consequences of firm behaviors. Five forms of corporate structures are of interest in the research: managers, shareholder, government, family, and foreign ownership. I list the original questions asked in Appendix A.

I consider individual and family the same form of corporate structure, as individual controlled firms are usually smaller and could grow into a family business later. Further, the questions are not totally congruent among the two data sets. The questions in PICS focus on the biggest shareholders in a firm. As I mention in the beginning of the dissertation, the biggest shareholders are assumed to be the final decision-makers of the firms because they can control the decision-makers of the company through voting. Therefore, the independent variables in the two data sets are still the same and suitable for this research.

## **Moderators**

### **Cultural Values**

The culture values in the dissertation are from the GLOBAL Leadership and Organizational Behavior Effectiveness (GLOBE) study (House et al., 2004). The researchers conduct a broad based, cross-country, cross industry research involving 62 societies. The intent of the study is to explore the cultural impacts on organizational practices and leadership attributes (House, Javidan, Janges, and Dorfman, 2002). Through thousands of surveys of middle managers in different nations, the researchers eventually identify nine cultural dimensions, which are uncertainty avoidance, power distance, societal collectivism, in-group collectivism, gender egalitarian, assertiveness, future orientation, performance orientation, and human orientation. The first six cultural dimensions are originally developed by Hofstede (1984). In their questionnaire items, the researchers divide the measure of culture values into “should be” judgment and “what is” judgment. The approach of “should be” judgment is based on the traditional assessment of anthropology and the approach of “what is” judgment grows out of psychological/behavioral tradition.

I include four of the nine cultural values in the study. Consistent with the study of Parboteeah, Cullen, and Lim (2004), I use the “should be” measures of cultural values.

Further, I use the adjusted scores for the GLOBE measures (House et al., 2004: 742-747).

The measures could more correctly reflect the cultural values as the culturally biased response patterns are deleted (i.e. Asian subjects avoiding extremes of a scale or Mediterranean cultures favoring the mid points of a scale). As Martin et al. (2006) also point out, only limited information is disclosed on the actual scale items included and the measure validation procedures in the GLOBE study. The information below is from the book *Culture, Leadership and Organization: The GLOBE Study of 62 Cultures* (House et al. 2004). Detailed and sample items of the cultural dimensions in the GLOBE study are located in Appendix B.

The conceptualization and measurement of performance orientation is developed by Trompenaars (1993), who views performance orientation as a contrast to social relations. The measure of this cultural dimension is composed of four items, and the GLOBE scholars report an alpha of .72. As to future orientation, it is derived from Kluckhohn and Strodtbeck's (1961) past, present, future orientation and the cultural value reflects the degree to which a society encourages and rewards such behaviors as planning, delaying gratification and investing in the future (House et al., 2002). The GLOBE study assesses the culture values with four items, and the cultural dimension is reliable at an alpha of .80. The societal in-group collectivism construct exclusively focuses on families, children,

and parents and assesses the degree to which individuals express pride, loyalty, and interdependence in their families (House et al., 2004). It also evaluates the extent to which others' work and accomplishments are considered honorable for the group as a whole (House et al., 2004). The cultural dimension values group cohesiveness and loyalty, also consistent with a conceptualization of a collectivist culture. The four-item measure is at an alpha of .77. The GLOBE measures of power distance reflect the extent to which a society maintains inequality among its members and groups in regards to power, authority, prestige, status, wealth, and material possessions (House et al., 2004). The measure of this cultural value is at organizational level and societal level, mainly concerned with the acceptance and endorsement of power difference among individuals. The alpha value of the cultural dimension in the GLOBAL study is .80.

### **Social Institutions**

**The Polity and Economy** This variable is primarily related to the degree that the state is involved in economic activity. Turner (1997) argues that nations whose political systems are redistributive-oriented have more governmental intervention, which is reflected in terms of governmental expenditures and governmental revenues. This argument is supported by Esping-Anderson (1990). Therefore, I use a measure of welfare socialism to evaluate polity and the economy. As developed by Cullen et al. (2004), there

are three items for this measure: governmental expenditure as a percentage of gross domestic product, government revenues as a percentage of gross domestic product, and tax collected as a percentage of gross domestic product. This data is collected from the World Bank's World Development Indicators. The three items are standardized and averaged to form the value of polity and the economy. The value of Cronbach's alpha for WBES (2000) data set is .979 and .912 for the data set of PICS.

**The Economy** Cross-national researchers view industrialization as a suitable indicator for the development of the economy. Scholars generally measure a nation's total energy use (e.g. Smits, Ultee, and Lammers, 1997) as the indicator because the shift from agriculture community to manufacturing-oriented society results in an increased demand in energy (Chenery and Syrquin, 1975). However, considering the theoretical argument from Turner (1997), it would be better to take into account the physical and human resource inputs and outputs that characterize an industrial economy. As a result, consistent with Cullen et al. (2004), I measure the economy with three items: the degree of urbanization (measured by the percentage of urban population, [Duch and Taylor, 1993]), energy use (kg of oil equivalent per capital, [Smits et al., 1997]), and the distribution of workforce that is located in non-agricultural sector (measured as percentage of workers in the non-agricultural sector [Temple and Voth, 1998]). Data were

collected from the World Bank World Development Indicators. The alpha value for the data set of WEBS (2000) is .855 and .715 for PICS.

**Political Constraints** I employ a commonly accepted measure of Political Constraint Index developed by Henisz (2000). The index is a structurally-derived internationally comparable measure of political constraints. Henisz's (2000) intention is to demonstrate the relationship between policy outcomes and the function of political structure. He argues that policy outcomes are a function of political structure, which is suitable for this study. If the political structure contributes to a more stable political environment then, firm deviance, such as bribery and tax evasion, is less likely to happen because the firms do not need to engage in deviant behaviors in order to avoid the uncertainty. There are three types of data to constitute the measure of political constraints: information in regards to the number of institutional players in a given polity, data on the alignments of parties, and data on the party composition of legislatures (Henise, 2000). The measure has been used extensively in international business studies (e.g. Delios & Henisz, 2000, 2003; Goerzen & Beamish, 2003; Henisz & Delios, 2001; Lu, 2002).

### **Control Variables**

**Gross National Income Per Capital** From the theoretical argument of anomie theory that suggests complex associations between cultural and social factors and deviant

behaviors, and in order to isolate the effect of national wealth on firm behavior, I control the variable of gross national income per capital. Some other studies (e.g., Wu, 2005) have found significant relationships between gross domestic product per capital and corruption. However, some might support the use of the index of national wealth as a whole rather than the per capital value. I argue that using per capital value could more accurately reflect the relationship between wealth and deviant behaviors. For instance, China has one of the highest GDP values in the world but low GDP per capital. Using GDP to investigate the relationship between wealth and wrongdoing in such a country might distort the real situation. The data used in the study is collected from the World Development Indicators and is log transformed prior to analysis.

**Firm Size** Firm size has proved to be related to firm level wrongdoing, which has been discussed in the section of literature review previously. Therefore, it is necessary to control this variable to isolate its influence. However, previous researchers have developed several measures of size, such as sales, assets, and number of workers, which are highly intercorrelated (Kimberly, 1976). As a result, I use the number of employees as the measure, which is the most common measure of size (Hall, 1987) and has been used in 80 percent of empirical studies in organization theory (Kimberly, 1976).



## **Analytical Tool**

**Hierarchical Linear Model** In this research, I focus on how firm level variables predict firm behaviors and how national factors moderate the relationship. This type of multi-level research has been referred to as either a cross-level (Rousseau, 1985) or mixed determinant (Klein, et al., 1994) model. I use Hierarchical Linear Model (HLM) (Bryk and Raudenbush, 1992) to conduct the data analysis, a recommended statistical tool to evaluate cross-level relationships.

Researchers rely on two applications of linear regression to conduct multi-level studies. The first method is data desegregation, in which every lower level unit is assigned a score representing the higher level unit within which it is nested (bring level 2 data down to level 1). The N used in regression to calculate coefficients is based on the total number of individual subjects. Using this method might face the issue that multiple individuals are exposed to similar group stimuli, which does not meet the traditional statistical approach assumption of the independence of observations (Bryk and Raudenbush, 1992). Furthermore, that the data are analyzed at the lower level would underestimate the value of standard errors and thus the risk of type one error is increased (Tate and Wongbundit, 1983).

The second method used by other researchers is data aggregation. One can examine

the relationship between levels by aggregating the individual results to the group level (all level 1 variables are summed up to level 2 by averaging). The potential problem within this method is that the individual level variance in the outcome measure is ignored. The second problem with using this method is that the interaction between lower level variables and higher level variables cannot be tested.

HLM is designed to overcome the disadvantages that the above two methods have. HLM allows one to simultaneously examine both the relationships within groups and between groups. Therefore, researchers need to estimate two models at the same time, one investigating relationships within each of the lower level units and the other one examining how those relationships vary across units. The situation of interdependence among individuals is thus reflected in HLM, while maintaining the appropriate level of analysis.

HLM is conducted as two-stage process (Hoffman, Griggin, and Gavin, 2000). At the first stage, HLM analyzes the relationships among individuals in the same group and calculates the intercept as well as slope within the unit. At second stage, the estimates of intercept and slope within each unit are then served as the outcome variables of the second level analysis, and HLM then analyzes the relationship between units. In other words, level 2 analyses treat variance in within-unit intercept as direct effect and variance

in within-unit slope as moderation effect.

The majority of organizational researchers have used traditional regression to conduct cross-level analysis, predicting outcome variable from both lower and higher level variables (Mossholder and Bedeian, 1983). Ordinary Least Squares is the approach to estimate the parameters under traditional regression, in which all of the regression parameters are fixed and the level 2 variance component is not separated from level 1. As to HLM, level 1 variables are allowed to vary across groups. The model uses a maximum likelihood estimation of the variance component, generalized least squares estimate for the level 2 parameters, and empirical Bayes estimates of the level 1 parameters (Bryk and Raudenbush, 1992).

In this dissertation, HLM analyzes my firm level variables and country level variables simultaneously. The variables in level 1 model include corporate structures, the dependent variable, corporate wrongdoing, the outcome variable, and company size, the control variable. The variables in level 2 model contain culture values and social institutions, which are moderators, and national income revenue per capital, the higher level control variable. The HLM model used is slope-as-outcome, which assumes that the moderation effect exists between the variables in different levels. As to the centering issue, Kreft, De Leeuw, and Aiken (1995:17) conclude that “there is no statistically

correct choice.” Group-centering method is used in level 1 and un-centered method is employed in level 2 analysis. Although HLM has been proved to be advantageous in multi-level analysis, it must be noted that HLM is not without limitations.

## **Chapter 5. Results**

The main purpose of this chapter is to report the test results of the hypotheses and some statistical related issues. There are three parts in the chapter. The first part is the descriptive statistics of the two data sets. In the second part, I discuss the variance components of the two data sets. The third part shows the results of the hypothesis tests.

### **Descriptive Statistics**

Table 4 and Table 5 are the descriptive statistics for the data sets of WBES and PICS respectively. The correlations and statistics are based on the data counterweighted by country sample size. The correlation between in-group collectivism and GNI per capital is -0.74, between future orientation and performance orientation is 0.74 in WBES, and between GNI per capital and the economy is 0.78 in PICS. Although the values are considered high, the variance inflation factors are less than 10 for all parameters in the two data sets, suggesting that multicollinearity is not an issue (Studenmund, 1992).

### **Variance Components between Levels**

In the study, I test firm-level and country-level independent variables on corporate wrongdoings. Before testing country-level factors, consistent with the methods discussed by Bryk and Raudenbush (1992:62), I need to find whether between-country level variation of tax evasion and bribery exists. It makes much less sense to conduct

country-level analysis if the differences among country-level means do not exist. These models are similar to ANOVA tests to decide whether between-country differences is larger than the within country differences (Bryk and Raudenbush, 1992:33). The variance components of the two data sets are listed in Table 6.

The within-country variance of tax evasion is 6.21 for WEBS and 500.25 for PICS; the between-country level variance for WBES is 0.85 and 52.00 for PICS. The intraclass correlation coefficients (ICC) of tax evasion are 0.12 and 0.09 for WEBS and PICS respectively, meaning that country-level variance explains 12% and 9% of the total variance of tax evasion in the two data sets. As to bribery, the firm-level variance is 0.87 for WEBS and 13.45 for PICS; the country-level variance is 0.79 of WEBS and 0.64 for PICS. The ICCs of bribery are 0.48 and 0.05 for WBES and PICS respectively. As I have mentioned in the beginning of the dissertation, due to the similarities among countries in PICS, the country-level variances in this data set is smaller than those in WBES. Further, all p-values for the four models are less than 0.000, meaning that the differences do exist for country-level means of tax evasion and bribery in both data sets, making the cross-level analysis in the study meaningful.

## **Hypothesis Testing**

In this section, I report the testing results of each hypothesis. At firm-level analysis, I set the alpha level at traditional 0.05. However, as to country-level analysis, because the number of countries is not as sufficient as it should have been, I set the alpha level at 0.1 in order to increase the statistical power. The firm-level results are listed from Table 7 to Table 11, and the consequences for country-level analyses are listed from Table 12 to Table 16.

### **Firm-level Hypotheses**

#### **Hypothesis 1a and 1b**

The hypothesis 1a and 1b state that manager-controlled firms are positively related to tax evasion and positively related to bribery respectively. The hypothesis 1a is supported by PICS at p-value smaller than 0.001, but not supported by WBES. As to bribery, the statistical results do not support the hypothesis 1b in both data sets (see Table 7).

#### **Hypothesis 2a and 2b**

Hypothesis 2a and 2b state that shareholder-controlled firms are negatively related to tax evasion and negatively related to bribery. Only the data set of WBES provides this information. However, there is no significant result in either of the two hypotheses.

Therefore, I am unable to draw any conclusions about supporting the hypotheses 2a and 2b (see Table 8).

### **Hypothesis 3a and 3b**

Hypothesis 3a and 3b state that government-controlled firms are negatively related to tax evasion and negatively related to bribery. In regards to tax evasion, the hypothesis 3a is well supported by the two data sets. The p-value is less than 0.05 in WBES and less than 0.001 in PICS. As to hypothesis 3b, both data sets show negative associations between government-controlled firms and bribery. However, only the result from PICS shows statistical significance ( $p \leq 0.05$ ) (see Table 9).

### **Hypothesis 4a and 4b**

Hypothesis 4a and 4b state that family-controlled corporations are positively related to tax evasion and positively related to bribery. The two hypotheses are well supported in both data sets. For the hypothesis 4a, the p-value in WBES is less than 0.05 and less than 0.01 in PICS. As to hypothesis 4b, the statistical result is significant at 0.05-level in WBES and at 0.001-level in PICS (see Table 10).

### **Hypothesis 5a and 5b**

Hypothesis 5a and 5b state that foreign-controlled firms are negatively related to tax evasion and negatively related to bribery. Only the data set of PICS has the information.



The results show that the two hypotheses have negative associations, but only the hypothesis 5a is statistically significant ( $p \leq 0.01$ ) (see Table 11).

### **National-level Hypotheses**

#### **Hypothesis 6a and 6b**

Hypothesis 6a and 6b state that the positive relationships between manager-controlled firms and tax evasion, and between manager-controlled firms and bribery, are enhanced by the increased culture value of performance orientation. The hypothesis 6a is well supported by the two data sets ( $p \leq 0.05$  in WBES,  $p \leq 0.1$  in PICS). However, hypothesis 6b is not supported by either of the two data sets. Therefore, there is no conclusion for me to draw for the hypothesis 6b (see Table 12).

#### **Hypothesis 7a and 7b**

Hypothesis 7a and 7b state that the negative relationships between shareholder-controlled firms and tax evasion, and between shareholder-controlled firms and bribery, are reduced by the increased culture value of performance orientation. In other words, I expect to find positive relationships in the two hypotheses. However, the statistical results from WBES reveal that the two hypotheses are not supported. Hence, I can not conclude that the culture value of performance orientation influences the associations between shareholder-controlled firms and corporate wrongdoings. The data

set of PICS does not have the information in regards to shareholder-controlled firms (see Table 13).

### **Hypothesis 8a and 8b**

Hypothesis 8a and 8b state that the positive relationships between manager-controlled firms and tax evasion, and between manager-controlled firms and bribery are reduced by the increased future-orientation culture value. I expect to find negative relationships in both hypotheses. However, the hypothesis 8a does not receive any statistical support from either of the two data sets. As to bribery, the hypothesis 8b is found supported by PICS ( $p \leq 0.05$ ) but not by WEBS (see Table 12).

### **Hypothesis 9a and 9b**

Hypothesis 9a and 9b state that the negative relationships between shareholder-controlled firms and tax evasion, and between shareholder-controlled firms and bribery, are enhanced by the increased cultural value of future orientation. However, in the data set of WBES, there is no statistical support for the two hypotheses (see Table 13).

### **Hypothesis 10a and 10b**

Hypothesis 10a and 10b state that the negative relationships between government-controlled firms and tax evasion, and between government-controlled firms

and bribery, are reduced by the increased value of in-group collectivism. I do not find statistical support for the hypothesis 10a. However, the hypothesis 10b is well supported in the two data sets. The p-value is less than 0.01 in WBES and less than 0.1 in PICS (see Table 14).

### **Hypothesis 11a and 11b**

Hypothesis 11a and 11b state that the positive relationships between family-controlled firms and tax evasion and between family-controlled firms and bribery, are enhanced by the increased value of in-group collectivism. The statistical results reveal that the hypothesis 11a is not supported by both data sets but that the hypothesis 11b is well supported by the two data sets. The hypothesis 11b is supported at p-value less than 0.05 in WBES and PICS (see Table 15).

### **Hypothesis 12a and 12b**

Hypothesis 12a and 12b state that the negative relationships between government-controlled firms and tax evasion, and between government-controlled firms and bribery, are reduced by the increased value of power distance. In other words, I expect to find positive relationships in the test results. However, the statistical results from the two data sets do not support the two hypotheses (see Table 14).

### **Hypothesis 13a and 13b**

Hypothesis 13a and 13b state that the positive relationships between family-controlled firms and tax evasion, and family-controlled firms and bribery, are enhanced by the increased culture value of power distance. Both hypotheses are supported by PICS but not by WBES. The p-values in PICS for the hypothesis 13a and 13b are less than 0.1 and 0.05 respectively (see Table 15).

### **Hypothesis 14a and 14b**

Hypothesis 14a and 14b state that the positive relationships between manager-controlled firms and tax evasion, and between manager-controlled firms and bribery, are reduced by increased welfare socialism. The two data sets do not support either of the two hypotheses. However, the hypothesis 14a is found positively related to tax evasion in both data sets (see Table 12).

### **Hypothesis 15a and 15b**

Hypothesis 15a and 15b state that the negative relationships between shareholder-controlled firms and tax evasion, and between shareholder-controlled firms and bribery, are enhanced by increased welfare socialism. The statistical results from WBES do not reveal any supportive finding for either of the two hypotheses. Therefore, no conclusion can be drawn with regards to hypothesis 15a and 15b (see Table 13).

### **Hypothesis 16a and 16b**

Hypothesis 16a and 16b state that the positive relationships between family-controlled firms and tax evasion, and between family-controlled firms and bribery, are reduced by increased welfare socialism. The analytical results from the two data sets do not support either of the two propositions. Further, the hypothesis 16a is found significant ( $p \leq 0.05$ ) at the opposite direction in WBES (see Table 15).

### **Hypothesis 17a and 17b**

Hypothesis 17a and 17b state that the negative relationships between foreign-controlled firms and tax evasion, and between foreign-controlled firms and bribery, are enhanced by increased welfare socialism. The statistical results from PICS do not reveal support for the two hypotheses. The data set of WBES does not provide the information (see Table 16).

### **Hypothesis 18a and 18b**

Hypothesis 18a and 18b state that the positive relationships between manager-controlled firms and tax evasion, and between manager-controlled firms and bribery, are enhanced by increased economic dominance. The analytical results in the two data sets do not reveal support for the two hypotheses. Therefore, I am unable to draw any conclusion from the findings (see Table 12).

### **Hypothesis 19a and 19b**

Hypothesis 19a and 19b state that the negative relationships between shareholder-controlled firms and tax evasion, and between shareholder-controlled firms and bribery, are reduced by increased economic dominance. I expect to find positive associations from the two hypotheses. However, the test results from WBES do not reveal any supportive findings (see Table 13).

### **Hypothesis 20a and 20b**

Hypothesis 20a and 20b state that the negative relationships between government-controlled firms and tax evasion, and between government-controlled firms and bribery, are reduced by increased economic dominance. Both hypotheses are well supported by the data set of WEBS and the p-values are both less than 0.01. However, the data set of PICS does not show any significant support for either of the two hypotheses (see Table 14).

### **Hypothesis 21a and 21b**

Hypothesis 21a and 21b state that the positive relationships between family-controlled companies and tax evasion, and between family-controlled companies and bribery, are enhanced by increased economic dominance. The data set of WBES does not reveal any statistical support for the two hypotheses. On the other hand, the data set

of PICS reveals support for the hypothesis 21a with p-value that is less than 0.05. As to the hypothesis 21b, I do not find any supportive finding in PICS (see Table 15).

### **Hypothesis 22a and 22b**

Hypothesis 22a and 22b state that the negative relationships between foreign-controlled firms and tax evasion, and between foreign-controlled firms and bribery, are reduced by increased economic dominance. The data set of PICS does not reveal any supportive evidence for the two hypotheses (see Table 16).

### **Hypothesis 23a and 23b**

Hypothesis 23a and 23b state that the positive relationships between manager-controlled firms and tax evasion, and between manager-controlled firms and bribery, are reduced by greater political constraints. The testing results from the two data sets of WBES and PICS do not reveal supportive findings for the two hypotheses (see Table 12).

### **Hypothesis 24a and 24b**

Hypothesis 24a and 24b state that the negative relationships between shareholder-controlled firms and tax evasion, and between shareholder-controlled firms and bribery, are enhanced by greater political constraints. However, the data set of PICS does not reveal significant statistical findings for the two hypotheses (see Table 13).

### **Hypothesis 25a and 25b**

Hypothesis 25a and 25b state that the positive relationships between family-controlled firms and tax evasion, and between family-controlled firms and bribery, are reduced with greater political constraints. The statistical results in the data set of WBES do not statistically support the two hypotheses. In PICS, the statistical findings do not support the hypothesis 26a, but support the hypothesis 25b with p-value that is less than 0.1 (see Table 15).

### **Hypothesis 26a and 26b**

Hypothesis 26a and 26b state that the negative relationships between foreign-controlled firms and tax evasion, and between foreign-controlled firms and bribery, are enhanced by greater political constraints. The hypothesis 26a is well supported by the data set of PICS, but the hypothesis 26b does not receive statistical support (see Table 16).



## **Chapter 6. Discussion**

In chapter 6, I discuss the results and implications for the research. There are four parts in the chapter. The first part is summary of the key findings from control variables, firm-level predictors, and country-level moderators. The second part is contributions and implications of the study. The third part is the discussion of limitations. The final part is the suggestions for future research.

### **Summary of the Key Findings**

#### **Control Variables**

There are two control variables in the study. The first one is firm size and the second one is gross national income (GNI) per capital. The control variable of firm size belongs to level-one factor and gross national income per capital is a national-level control variable. In previous studies (e.g. Baucus, 1994), researchers do not reach a consensus in regards to the association between firm size and corporate wrongdoings. For instance, Simpson (1986) finds that large companies are more likely to be illegal but Cohen (1992) has the opposite conclusion. In this dissertation, I find that firm size is consistently negatively related to both tax evasion and bribery (see Table 7 to 16), and the majority of the findings are statistically significant. Based on the argument of Mckendall and Wanger (1997), these results may be due to the fact that bigger firms' behaviors are more visible

and likely to attract attention, thus reducing the propensities of companies to be deviant.

As to country-level control variable of GNI per capital, the results in the study do not reveal consistent findings (see Table 12 to 16). The control variable does not have significant moderating impact on the relationships between shareholder-controlled firms and corporate wrongdoings, between family-controlled firms and corporate wrongdoings, or between foreign-controlled firms and corporate wrongdoings. On the other hand, GNI per capital is negatively related to the associations between manager-controlled firms and bribery, and negatively related to the association between government-controlled firms and tax evasion, but positively related to the association between government-controlled firms and bribery. Interestingly, based on previous research, the conflicting findings in this study are not anticipated. The general conclusions from previous studies suggest that GNI per capital is negatively related to corporate deviance (Wu, 2005). Countries with a better economical development could reduce individual-level deviance. However, previous studies mostly focus on the main effect but not on the moderating effects examined in this research. Therefore, more studies on this aspect are highly required.

### **Firm-level Variables**

There are 5 different forms of corporate controls in the study: manager-controlled firms, shareholder-controlled firms, government-controlled firms, family-controlled firms,

and foreign-controlled firms. Results from the study reveal that manager-controlled firms are positively related to tax evasion but negatively associated with bribery. The hypotheses that shareholder-controlled firms negatively relate to corporate wrongdoings are not supported. Government-controlled firms are negatively related to both tax evasion and bribery. As to family-controlled firms, they are found to be positively related to tax evasion and positively related to bribery. Foreign-controlled firms are found to be negatively related to tax evasion, but not related to bribery.

Some of the findings in the study are unexpected. The negative relationship between manager-controlled firms and bribery is surprising. I expect managers to engage in bribery in order to obtain short-term interests. However, the benefits of engaging in bribery might not be obtained in short term. Although bribery could circumvent bureaucratic systems and thus save some time for firms, companies need to build up solid and effective relationships with governmental officials before engaging in such behavior. Therefore, the time that needs to be invested before bribery and the time that the companies have to wait for the profits after bribery might be longer than managers expect. The situation might thus reduce the incentive for managers to bribe.

Although negative associations between shareholder-controlled firms and corporate wrongdoings are found, the statistical results are not significant. The reason for the

findings might be due to the lack of detailed information in regards to the structure of the boards. For further understanding, we need to know whether the boards of the directors are inside board of directors (insiders) or outside board of directors (outsiders). The major difference between insiders and outsiders is that insiders are also part of the management of the company. While insiders have more information in association with the firm's operations to enact policies, outsiders do not have access to sufficient information to make their decisions; outsiders base their decisions on readily available financial information (Lorsch and MacIver, 1989). Usually, the financial information only reflects a company's past, present, or short-term future performance (Hoskisson, Hitt, Johnson, and Grossman, 2002). On the other hand, inside directors understand more about the firm's internal and external environments, helping them to make more effective decisions (Lorsch and MacIver, 1989) which are usually long-term oriented. As a result, if the companies have more outside directors, the long-term oriented characteristics of shareholder-controlled firms would be offset. In other words, the proposed negative relationships between shareholder-controlled firms and corporate wrongdoings would become weaker.

As to government-controlled firms and family-controlled firms, the statistical findings of their associations with corporate wrongdoings are as expected. The

relationship between foreign-controlled firms and tax evasion is found to be significant as proposed, but foreign-controlled companies are not negatively related to bribery. One possible explanation for this situation lies in the characteristics of the PICS data set. Countries in the data set of PICS are mainly at premature stage of economic development. The business environment in those countries is not as well established as it is in the developed world. Legal systems, governmental regulations, and infrastructures in these countries are not equipped. In the words, foreign firms running businesses in these countries would encounter numerous unexpected difficulties. Hence, engaging in bribery in order to remove those obstacles becomes more necessary. In addition, the lack of regulations and laws would also reduce the chance of being detected, stimulating the behavior of bribery. As a result, the proposed negative relationship between foreign-controlled firms and bribery is not significantly supported.

### **National-level Variables**

I analyze the moderating effects based on anomie theory, established by Robert Merton. He argues that a society overemphasizing its goals would ignore the means to reach the ends. The situation would give people anomic pressure to engage in deviant behaviors. After several decades, Messner and Rosenfeld (1994) point out the importance of social institutions, which could also influence on individual's behaviors. Their main

argument is that the dominance of the economy would weaken the traditional social controls which are based on family or education. The result of the situation is the increase of deviance. This theory examines individuals' behaviors from culture values and social institutions that provide a solid theoretical foundation for the research of corporate deviance in this study.

### **Cultural Values**

Results reveal that performance orientation value positively moderates the relationship between manager-controlled firms and tax evasion, but has no moderating effect on the relationship between manager-controlled firms and bribery. In addition, I find no moderating effect of the same culture value on the relationships between shareholder-controlled firms and corporate wrongdoings, including tax evasion and bribery. As discussed previously, performance orientation might press managers to be deviant. However, bribing might take longer than expected. Therefore, the moderating effect is not salient.

For the non-significant moderating effect of performance orientation on the relationship between shareholder-controlled firms and corporate wrongdoings, a board could have outsiders and insiders. The performance evaluation of insiders is usually more objective because they also part of the management. Firms are more likely to use

financial reports to evaluate insiders' performances. As to outsiders, it is not easy to measure their performance. Their hiring is often based on their reputation. Therefore, their performance is rather subjective. If the directors of a board are mixed, the results are not likely to be supported statistically.

Statistical results reveal that the culture value of future orientation negatively moderates the relationship between manager-controlled firms and bribery, but the relationships between manager-controlled firms and tax evasion and between shareholder-controlled firms and corporate wrongdoings are not found to be significant. With regards to the non-significant findings pertaining to the association between shareholder-controlled firms and corporate wrongdoings, the reason for the results may still lie in the boards of directors' backgrounds. Inside boards of directors have more thorough knowledge about the company; they tend to make long-term oriented decisions. Outside boards of directors are less familiar with the company; they are unable to consider the detailed operation of the firm to make their decisions. Therefore, outsiders are inclined to make short-term oriented decisions. Although I propose that future orientation would have a negative moderating effect, the results seem to imply that the influence from culture is not larger than the influence of the decision-makers' backgrounds.

Statistical results reveal that the cultural value of in-group collectivism positively moderates the relationships between government-controlled firms and bribery, and between family-controlled firms and bribery. However, no significant moderating effect is found in either the relationship between government-controlled firms and tax evasion, or the relationship between family-controlled firms and tax evasion. It is fairly interesting that the cultural value is consistently able to predict bribery but not tax evasion. The outcomes may lie in bribery's people-oriented characteristics. Based on the definitions of tax evasion and bribery, bribing seems to need more people to be involved to finish the behavior. The cultural value of in-group collectivism emphasizes the relationships between an individual and his/her groups. People not only depend on their close groups but also need to maintain harmony with them. House et al. (2004) suggest that the interactions among people affected by the value are longer and more intimate. The implication of the situation is that people affected by high in-group collectivism could thus have more direct or indirect relationships among one another, which could be a big help when people engage in bribery. As a result, the characteristic of the people-oriented cultural value may offer a stronger power to predict bribery.

The statistical findings reveal that the power distance value negatively moderates the relationships between government-controlled firms and corporate wrongdoings, but



positively moderates the relationships between family-controlled firms and corporate wrongdoings. The conflicting findings are rather surprising. Power distance refers to the degree to which people are willing to accept inequity between different levels. Affected by high power distance value, people are more likely to accept power inequity between them and their supervisors, and the implications for that is that people would have more tolerance for and engage in deviant behaviors. The unexpected outcomes suggest the need to pay attention to the organizations' characteristics, which might influence the moderating effect. For government-controlled firms, they are more likely to have clear regulations with regards to individuals' responsibilities and the use of authorities, which is often understood as bureaucracy. Perhaps the bureaucratic system of government-controlled firms would be strengthened affected by high power distance value, which means that people would just follow the rules to make their decisions and that decision-makers are less inclined to be deviant. However, before drawing any solid or convincing conclusion, more studies are needed in order to understand the factors to cause the interesting results.

### **Social Institutions**

Three different kinds of social institutions are tested for their moderating effects.

The three social institutions are the polity and economy, the economy, and political

constraints. The results reveal that only very few hypotheses in this part are supported.

The few supported hypotheses would make it challenging to draw any solid or satisfying conclusion.

From the perspective of anomie theory, there might be one explanation for the situation. Robert Merton (1938) argues that a society that over emphasizes its goal would ignore the means to reach those goals; the consequence of the emphasis is deviance. Merton focuses on the influence of cultures but not the influence of social institutions, which is criticized by later researchers. Messner and Rosenfeld (2001; Rosenfeld and Messner, 1997) argue that Merton does not pay sufficient attention to the institutional drivers of anomie. Although Merton does not mention the influence of social institution, this wise man perhaps has already noticed about the limited influence of social institutions. In his opinion, the cause of deviant behavior lies in the characteristics of cultural values. Cultural values would give people anomic pressure if they over focus the ends. The situation is perceptual. Furthermore, Merton does not agree with Durkheim who argues that anomie comes from the sudden change of social institutions. Therefore, from Merton's point of view, the impact from social institutions is supposed to be little. The findings in the results do partially reflect his thoughts.

Another explanation may lie in the measure of social institutions. I use the original

existing indexes or follow the methods employed in previous studies to measure social institutions. For instance, the measure of the polity and economy is composed of three items, governmental expenditure as a percentage of GDP, government revenues as a percentage of GDP, and tax collected as a percentage of GDP. The above three-measures represents the strength of the welfare socialism. I hypothesize that high welfare socialism would bring a negative moderating effect. However, the social institution positively moderates the relationship between family-controlled firms and tax evasion. The item of tax collection could be the reason for the result. A high percent of tax collection of GDP could force firms to evade tax. The measure of welfare socialism may thus cause the opposite results, which are unexpected. As a result, substituting the item with a suitable one to measure welfare socialism could help us have a clear picture of the association.

### **Contributions and Implications**

This study makes two key contributions to the academic world. First, the research takes into account the decision-making mechanism of a firm to examine its relationships with firm deviant behaviors. In previous studies, researchers mainly focused on firm characteristics, such as firm size, to investigate this issue. There has been no consensus among researchers so far. In other words, other potential factors might also influence the dependent variables; considering the backgrounds of firms' decision-makers becomes

necessary and should not be ignored. For instance, agency theory suggests that managers are self-interest oriented and likely to pursue their own benefits at the costs of the shareholders, suggesting that manager-controlled firms are more inclined to be deviant. Further, the application of deterrence theory suggests that family-controlled firms positively relate to corporate wrongdoings and that foreign-controlled firms negatively related to firm deviance. The above examples help us understand what firm characteristics might be the drivers for deviant behaviors. This dissertation differentiates corporate controls into five different forms and each has its own uniqueness. Every type of corporate control has different propensities to be deviant. We could thus be able to predict firms' wrongdoings from their forms of control. The statistical findings in this regard are listed in the Appendix (Table 7 to Table 11).

The second contribution by the study is that it reflects the importance of national factors, which would moderate the associations between forms of firm control and the organizational deviance. In other words, the same forms of corporate control might have different propensities to be deviant under the influence of cultural values and social institutions. The theoretical argument is based on Merton's anomie theory and is consistent with Baucus's (1994) argument that company performance is attributed to more than a single factor. A firm's characteristics, such as strategy, structure, and the

environment, should be taken into consideration. Although past studies (e.g. Martin et al. 2006) also examine the influence of national factors, the researchers only consider the main effects without the influence of moderating effects. This study is thus able to fill the gap.

The practical implications of the study are important. Given that corporate scandals are becoming more and more prevalent, how to avoid and deal with them is every government's key concern. This study provides big directions for governments to cope with the problems. For instance, the results reveal that family-controlled firms have a stronger propensity to bribe under higher in-group collectivism. Further, under high performance orientation, government should pay more attention to manager-controlled firms because they are more likely to evade tax. Given these findings, a government can therefore enact effective regulations to reduce such firm deviance or to prevent such corporate wrongdoings from happening.

### **Limitations**

There are several limitations in the study. First, the two data sets are all secondary data. It is a well-known limiting factor to a study. We are unable to know the extent to which the processes to collect the information are adequate or not.

Furthermore, the characteristics of the data sets might explain why the findings are

not consistent between the two data sets. For instance, the data set of WEBS is composed of nations from different stages of economic development. The differences between culture values and social institutions are great among these nations. The ICCs of tax evasion and bribery in the data set of WEBS are 0.12 and 0.48 respectively, meaning that national factors explain 12% and 48% of the total variance of the two corporate wrongdoings. On the other hand, the nations in the data set of PICS are at more similar stage of economic development. Therefore, there is less country-level variance among these nations. The ICCs of tax evasion and bribery are 0.09 and 0.05 respectively, which means that there is not too much country-level difference among these nations.

In addition, it is possible to assume that certain relationships between different forms of corporate controls and corporate wrongdoings are not linear and perhaps are non-linear. This would explain why some findings in the study are significant in the opposite direction.

There is by no means a complete study of the drivers of the moderating effects from national factors. For instance, there are 9 culture values in the GLOBE study. However, drawing from anomie theory, I include only 4 culture values in these models. The same argument can be applied to social institutions. The study is thus only a partial explanation, like most other studies, but it is indeed a contributive and intriguing one.

## **Recommendations for Future Research**

Future research could be viewed from firm level and national levels. From firm level, researchers should investigate other forms of corporate controls. There are only five different forms of control discussed in the study. Other possible forms of controls should be examined. For instance, joint venture is a very popular entry mode for a foreign firm. The propensities for foreign-firms to be deviant may vary depending upon the amount of local shares. In addition, employers can be the firms' controllers. How these worker-controlled firms behavior might be interesting.

At the national level, based on anomie theory, future research should include different cultural values and social institutions. Although statistical results do not show too much support for the moderating effects of social institutions in the studies, we cannot thus deny or ignore their potential influence as we have not yet explored all the national variables.

A third recommendation for future research direction is a longitudinal study. Cultural values or social institutions within a country might change as time goes on. Such studies would assess how the moderating effects change the relationships between forms of corporate controls and organizational deviance.

Other potential research questions include different kinds of corporate deviance. For

instance, inside trade is one serious issue in business now; possibilities for firm-level drivers and country-level drivers, as moderators, should also be examined in the future.



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## Appendix A

### The Measure of Dependent and Independent Variables

#### Dependent Variables

Tax Evasion

WEBS (2000)

Recognizing the difficulties many enterprises face in fully complying with taxes and regulations, what percentage of total sales would you estimate the typical firm in your area of activity keeps “off the books?”

- a) None at all
- b) 1-10 %
- c) 11-20%
- d) 21-30%
- e) 31-40%
- f) 41-50%
- g) More than 50% (specify \_\_\_\_ %)

PICS

Recognizing the difficulties many enterprises face in fully complying with taxes and regulations, what percentage of total sales would you estimate the typical establishment in your area of activity reports for purposes?

Bribery

WEBS (2000)

When firms in your industry do business with the government, how much of the contract value must they offer in additional or unofficial payments to secure the contract?

- 1) 0%
- 2) Up to 5%
- 3) 6-10%
- 4) 11-15%
- 5) 16-20%
- 6) Greater than 20% (specify \_\_\_\_\_%)

DK Don't know

PICS

We've heard that establishments are sometimes required to make gifts or informal payments to public officials to "get things done" with regard to customs, taxes, licenses, regulations, services etc. On average, what percent of annual sales value would such expenses cost a typical firm like yours?

#### Independent Variables

##### WEBS (2000)

Which of the following best describe the overall control of your firm, where control means making major decisions concerning the enterprise's direction? (allow only once choice)

My firm is controlled by:

- a) Individual owner(s)
- b) A family
- c) A company group (conglomerate)
- d) A bank
- e) Its board of directors/supervisory board
- f) Its managers
- g) Its workers
- h) Government
- i) Other (specify)

##### PICS

Which of the following best describes the largest shareholder or owner in your firm?

- 1. Individual
- 2. Family
- 3. Domestic
- 4. Foreign company
- 5. Bank
- 6. Investment fund
- 7. Managers of the firm
- 8. Employees of the firm
- 9. Government or government agency
- 10. Other (Specify)



## Appendix B

### Cultural Measures of the GLOBE Study

(Unless indicated, all items 1 = strongly agree, 7 = strongly disagree)

#### Performance Orientation ( $\alpha = .72$ )

1. I believe that teen-aged students should be encouraged to strive for continuously improved performance (reverse scored).
2. In this society, major rewards are based on only performance effectiveness.
3. In this organization, employees should be encouraged to strive for continuously improved performance (reverse scored).
4. I believe that people should set challenging goals for themselves.

#### Future Orientation ( $\alpha = .80$ )

1. I believe that the accepted norm is to: (reverse scored):  
(Plan for the future/Accept the status quo)
2. I believe that people who are successful should: (reverse scored):  
(Plan ahead/Take life events as they occur)
3. In this organization, the accepted norm should be to: (reverse scored):  
(Plan for the future/Accept the status quo)
4. In this organization, people should:  
(Worry about current crises/Plan for the future)

#### Assertiveness ( $\alpha = .75$ )

1. In this society, people should be encouraged to be: (reverse scored):  
(Assertive/Nonassertive)
2. In this society, people should be encouraged to be: (reverse scored):  
(Tough/Tender)
3. In this organization, people should be encouraged to be: (reverse scored):  
(Dominant/Nondominant)
4. In the organization, people should be encouraged to be: (reverse scored):  
(Tough/Tender)

#### In-Group Collectivism ( $\alpha = .77$ )

1. In this society, children should take pride in the individual accomplishments of their parents (reverse scored).
2. In this society, parents should take pride in the individual accomplishments of their children.

3. In this organization, group members should take pride in the individual accomplishment of their group.

In this organization, group managers should take pride in the individual accomplishments of group members.

Power Distance ( $\alpha = .80$ )

1. I believe that followers should: (reverse scored):  
(Obey their leader without question/Question their leader when in disagreement)
2. I believe that power should be: (reverse scored):  
(Concentrated at the top/Shared throughout the society)
3. In this organization, subordinates should: (reverse scored):  
(Obey their boss without question/Question their boss when in disagreement)
4. In this organization, rank and position in the hierarchy should have special privileges: (reverse scored).

Human Orientation ( $\alpha = .88$ )

1. In this society, people should be encouraged to be (reverse scored):  
(Very concerned about others/Not at all concerned about others).
2. In this society people should be encouraged to be (reverse scored):  
(Very sensitive toward others/Not at all sensitive toward others).
3. In this organization, people should be encouraged to be (reverse scored):  
(Very concerned about others/Not at all concerned about others).
4. In this organization, people should be encouraged to be (reverse scored):  
(Very sensitive toward others/Not at all sensitive toward others).

Uncertainty Avoidance ( $\alpha = .88$ )

1. I believe that orderliness and consistency should be stressed, even at the expense of experimentation and innovation (reverse scored).
2. I believe that societal requirements and instructions should be spelled out in detail so citizens know what they are expected to do.
3. In this organization, orderliness and consistency should be stressed, even at the expense of experimentation and innovation (reverse scored).
4. In this organization, job requirements and instructions should be spelled out in detail so employees know what they are expected to do (reverse scored).

**Table 1**

The selection of national factors as moderators

	Manager-control Firms	Shareholder-control Firms	Government-control Firms	Family-control Firms	Foreign-control Firms
Cultural Values					
Performance Orientation	X	X			
Future Orientation	X	X			
In-Group Collectivism			X	X	
Power Distance			X	X	
Social Institutions					
Polity and the Economy	X	X		X	X
The Economy	X	X	X	X	X
Political Constraints	X	X		X	X

**Table 2**

Number of firms in each country in the data set of WEBS (2000)

<b>Country</b>	<b>Firm number</b>
Argentina	100
Brazil	201
Canada	101
Colombia	101
Costa Rica	100
Ecuador	100
El Salvador	104
France	100
Georgia	100
Germany	129
Guatemala	100
Hungary	106
Indonesia	129
Italy	100
Kazakhstan	127
Malaysia	100
Mexico	100
Philippines	100
Poland	225
Portugal	100
Russia	525
Singapore	100
Slovenia	125
Spain	104
Sweden	102
Turkey	150
UK	102
USA	100
Venezuela	100

**Table 3**

Number of firms in each country in the data set of PICS

<b>Country</b>	<b>Firm number</b>
Albania	374
Egypt	977
El Salvador	465
Georgia	374
Germany	1,196
Greece	546
Hungary	860
Indonesia	713
Ireland	501
Kazakhstan	835
Korea	598
Philippines	716
Poland	1,583
Portugal	505
Russia	1,107
Slovenia	411
South Africa	603
Spain	606
Turkey	1,071

**Table 4**Descriptive Statistics and Cross-Level Correlations for WBES (2000) <sup>a</sup>

Variables	Mean	s.d.	1	2	3	4	5	6	7	8
Firm level										
1. Bribery	2.25	1.26	1							
2. Tax Evasion	3.36	2.63	0.08**	1						
3. Size	1.82	0.71	-0.11**	-0.08**	1					
4. BOD	0.33	0.47	-0.1**	-0.06**	0.29**	1				
5. Manager	0.1	0.3	-0.09**	0.03	0.05**	-0.24**	1			
6. Government	0.02	0.14	0.09**	-0.05	0.08**	-0.1**	-0.05**	1		
7. Family	0.43	0.5	0.14**	0.07	-0.41	-0.62**	-0.29**	-0.13**	1	
Country-level										
8. In-Group	0.14	0.93	0.39**	0.07**	-0.01	-0.04*	-0.05**	0.08**	0.06**	1
9. Future Orientation	-0.22	1.02	-0.38**	0.01	0.04**	0.01	0.09**	-0.02	-0.06**	-0.58**
10. Performance Orientation	-0.17	0.97	-0.29**	0.01	0.08**	0.02	0.13**	-0.08**	-0.08**	-0.36**
11. Power Distance	0.14	0.98	0.12**	-0.02	-0.06**	-0.07	-0.01	0.05**	0.06**	0.28**
12. Political Constraints	-0.22	1.05	-0.33**	-0.09**	0.06**	0.03	0.04*	-0.06**	-0.05**	-0.37**
13. Polity and the Economy	-0.04	0.93	-0.21**	-0.12**	-0.03**	0.02	0.06**	-0.02	-0.02	-0.48
14. The Economy	-0.02	0.91	-0.22**	-0.12**	-0.03**	0.01	0.01	-0.07**	-0.03*	-0.49
15. GNI per Capital	-0.14	0.93	-0.47**	-0.15**	-0.02	0.05**	0.07**	-0.09**	-0.09*	-0.74**

Variables	Mean	s.d.	9	10	11	12	13	14	15	
Country-level										
9. Future	-0.22	1.02	1							
10. Performance Orientation	-0.17	0.97	0.74**	1						
11. Power Distance	0.14	0.98	-0.54**	-0.54**	1					
12. Political Constraints	-0.22	1.05	0.17**	0.12**	-0.11**	1				
13. Polity and the Economy	-0.04	0.93	0.23**	-0.05**	-0.06**	0.38**	1			
14. The Economy	-0.02	0.91	0.22*	0.1**	0.09**	0.12**	0.46**	1		
15. GNI per capital	-0.14	0.91	0.52**	0.39**	-0.17**	0.54**	0.61**	0.67**	1	

<sup>a</sup> n = 3,731, level 1; n = 29, level 2. All national variables are standardized. Correlations computed by assigning national-level variables to each firm within that firm.

<sup>b</sup> Gross National Income per capital is log transformed before standardized.

\*\* . Correlation is significant at the 0,01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

**Table 5**

## Descriptive Statistics and Cross-Level Correlations for PICS

Variables	Mean	s.d.	1	2	3	4	5	6	7	8
Firm level										
1. Bribery	0.99	3.74	1							
2. Tax Evasion	13.54	23.36	0.15**	1						
3. Size	1.72	0.8	-0.01	-0.05**	1					
4. Manager	0.03	0.18	0.01	0.08**	0.01	1				
5. Government	0.05	0.22	-0.04**	-0.07**	0.18***	-0.04*	1			
6. Family	.074	0.44	0.04**	0.03**	-0.4**	-0.32**	-0.39**	1		
7. Foreign	0.07	0.26	-0.02	-0.05**	0.25**	-0.05*	-0.07**	-0.47**	1	
Country-level										
8. In-Group	-0.01	0.83	-0.41**	-0.02**	0.04**	0.05**	-0.01	-0.08**	0.02*	1
9. Future Orientation	-0.07	1.00	0.03**	0.13**	0.1**	0.08**	-0.04**	-0.05**	0.03**	0.34**
10. Performance Orientation	-0.03	0.93	-0.06**	-0.14**	-0.06**	-0.00	-0.06**	0.00	0.01	0.41**
11. Power Distance	0.09	0.96	0.11**	0.01**	-0.04**	-0.07**	0.07**	0.03**	-0.05**	-0.3**
12. Political Constraints	-0.06	0.99	-0.11**	-0.1**	-0.11**	0.11*	-0.06**	-0.03**	0.03**	0.32**
13. Polity and the Economy	0.04	0.9	-0.1**	-0.16**	-0.14**	-0.12**	-0.02**	0.07**	0.01	-0.08**
14. The Economy	0.1	0.99	-0.15**	-0.23**	-0.18**	-0.18**	0.01	-0.02**	-0.02**	0.11**
15. GNI per capital	0.01	0.92	-0.16**	-0.24**	-0.23*	-0.16**	-0.05**	-0.04**	-0.04**	-0.01**



Variables	Mean	s.d.	9	10	11	12	13	14	15	
Country-level										
9. Future Orientation	-0.19	1.03	1							
10. Performance Orientation	0.23	0.85	-0.28**	1						
11. Power Distance	0.01	0.92	-0.45**	-0.04**	1					
12. Political Constraints	0.05	0.95	-0.04**	0.59**	-0.37**	1				
13. Polity and the Economy	0.1	0.98	-0.19**	0.45**	-0.14**	0.47**	1			
14. The Economy	0.39	0.85	-0.24**	0.31**	-0.29**	0.23**	0.39**	1		
15. GNI per capital	0.25	0.89	-0.36**	0.49**	-0.31**	0.55**	0.62**	0.78**	1	

<sup>a</sup> n = 14,041, level 1; n = 19, level 2. All national variables are standardized. Correlations computed by assigning national-level variables to each firm within that firm.

<sup>b</sup> Gross National Income per capital is log transformed before standardized.

\*\* . Correlation is significant at the 0,01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

**Table 6**

Variance components of each model in the two data sets

WBES				
	Level 1 variance	Level 2 variance	ICC <sup>a</sup>	P-value
Tax Evasion	6.21	0.85	0.12	< 0.000
Bribery	0.87	0.79	0.48	< 0.000
PICS				
	Level 1 variance	Level 2 variance	ICC	P-value
Tax Evasion	500.25	52	0.09	< 0.000
Bribery	13.45	0.64	0.05	< 0.000

<sup>a</sup>Intraclass Correlation Coefficient (ICC) measures the proportion of the variance in the outcome that is between country units. The value is calculated by the level 2 variance divided by the sum of level 1 and level 2 variance.

**Table 7**

HLM for Manager-controlled Firms – Model 1

Model 1	WBES		PICS	
Firm Level Variables	Tax Evasion	Bribery	Tax Evasion	Bribery
Control Variable				
Firm Size	-0.35****	-0.06*	-3.5***	-0.17***
Independent Variable				
Manager-controlled Firms	0.23	-0.01	4.54***	-0.43*
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
Performance Orientation*Manager				
Future Orientation*Manager				
Social Institutions				
The Polity and Economy* Manager				
The Economy* Manager				
Political Constraints* Manager				
Control Variable				
Gross National Income Per Capital* Manager				

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29

Level 2: n = 19

\*  $P \leq 0.05$     \*\*  $P \leq 0.01$     \*\*\*  $P \leq 0.001$

**Table 8**

HLM for Shareholder-controlled Firms – Model 1

Model 1	WBES	
Firm Level Variables	Tax Evasion	Bribery
Control Variable		
Firm Size	-0.33***	-0.05
Independent Variable		
BOD-controlled Firms	-0.11	-0.07
Interaction between Country Level Variables and Independent Variable		
Cultural Variables		
Future Orientation*BOD		
Performance Orientation*BOD		
Social Institutions		
The Polity and Economy*BOD		
The Economy*BOD		
Political Constraints*BOD		
Control Variable		
Gross National Income Per Capital*BOD		

WBES Level 1: n = 3,731

Level 2: n = 29

\*  $P \leq 0.05$     \*\*  $P \leq 0.01$     \*\*\*  $P \leq 0.001$

**Table 9**

HLM for Government-controlled Firms–Model1

Model 1	WBES		PICS	
Firm Level Variables	Tax Evasion	Bribery	Tax Evasion	Bribery
Control Variable				
Firm Size	-0.33***	-0.06**	-3.15***	-0.12**
Independent Variable				
Government-controlled Firms	-0.71*	-0.05	-6.5***	-0.67***
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
In-Group Collectivism* Government				
Power Distance* Government				
Social Institutions				
The Economy* Government				
Control Variable				
Gross National Income Per Capital* Government				

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29                      Level 2: n = 19

\*  $P \leq 0.05$     \*\*  $P \leq 0.01$     \*\*\*  $P \leq 0.001$

**Table 10**

HLM for Family-controlled Firms – Model 1

Model 1	WBES		PICS	
Firm Level Variables	Tax Evasion	Bribery	Tax Evasion	Bribery
Control Variable				
Firm Size	-0.3***	-0.04*	-3.25***	-0.09*
Independent Variable				
Family-controlled Firms	0.19*	0.08*	1.43**	0.35***
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
In-Group Collectivism* Family				
Power Distance* Family				
Social Institutions				
The Polity and Economy* Family				
The Economy* Family				
Political Constraints* Family				
Control Variable				
Gross National Income Per Capital* Family				

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29                      Level 2: n = 19

\*  $P \leq 0.05$     \*\*  $P \leq 0.01$     \*\*\*  $P \leq 0.001$

**Table 11**

HLM for Foreign-controlled Firms – Model 1

Model 1	PICS	
Firm Level Variables	Tax Evasion	Bribery
Control Variable		
Firm Size	-3.34***	-0.16**
Independent Variable		
Foreign-controlled Firms	-2.51**	-0.03
Interaction between Country Level Variables and Independent Variable		
Social Institutions		
The Polity and Economy* Foreign		
The Economy* Foreign		
Political Constraints* Foreign		
Control Variable		
Gross National Income Per Capital* Foreign		

PICS Level 1: n = 14,041

Level 2: n = 19

\*  $P \leq 0.05$     \*\*  $P \leq 0.01$     \*\*\*  $P \leq 0.001$

**Table 12**

HLM for Manager-controlled Firms – Model 2

Model 2	WBES		PICS	
	Tax Evasion	Bribery	Tax Evasion	Bribery
Firm Level Variables				
Control Variable				
Firm Size	-0.35	-0.06*	-3.47***	-0.17***
Independent Variable				
Manager-controlled Firms	0.09	0.01	2.47	-0.28*
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
Performance Orientation*Manager	0.63**	-0.16	5.61*	-0.22
Future Orientation*Manager	0.08	0.11	3.87	-0.27**
Social Institutions				
The Polity and Economy* Manager	0.04	-0.06	0.53	0.2*
The Economy* Manager	-0.24*	-0.08	5.35	0.32
Political Constraints* Manager	0.25	-0.05	-4.72	0.28**
Control Variable				
Gross National Income Per Capital* Manager	-0.28	0.03	1.01	-0.49*

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29

Level 2: n = 19

\* P ≤ 0.1    \*\* P ≤ 0.05    \*\*\* P ≤ 0.01



**Table 13**

HLM for Shareholder-controlled Firms – Model 2

Model 2	WBES	
Firm Level Variables	Tax Evasion	Bribery
Control Variable		
Firm Size	-0.32***	-0.05*
Independent Variable		
BOD-controlled Firms	0.05	-0.07
Interaction between Country Level Variables and Independent Variable		
Cultural Variables		
Performance Orientation*BOD	0.01	-0.11
Future Orientation*BOD	0.05	0.15
Social Institutions		
The Polity and Economy*BOD	-0.16	0.06
The Economy*BOD	0.1	-0.04
Political Constraints*BOD	0.27**	-0.06
Control Variable		
Gross National Income Per Capital*BOD	-0.13	0.02

WBES Level 1: n = 3,731

Level 2: n = 29

\*  $P \leq 0.1$  \*\*  $P \leq 0.05$  \*\*\*  $P \leq 0.01$

**Table 14**

HLM for Government-controlled Firms–Model2

Model 2	WBES		PICS	
	Tax Evasion	Bribery	Tax Evasion	Bribery
Firm Level Variables				
Control Variable				
Firm Size	-0.33***	-0.06**	-3.1***	-0.13***
Independent Variable				
Government-controlled Firms	-0.65	-0.01	-5.33*	-0.63***
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
In-Group Collectivism* Government	0.4	0.86***	-0.68	0.2*
Power Distance* Government	-0.32	-0.27***	-2.27**	-0.03
Social Institutions				
The Economy* Government	0.65***	0.18***	-1.85	0.07
Control Variable				
Gross National Income Per Capital* Government	0.02	0.29**	-5.97***	0.18*

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29                      Level 2: n = 19

\* P ≤ 0.1    \*\* P ≤ 0.05    \*\*\* P ≤ 0.01

**Table 15**

HLM for Family-controlled Firms – Model 2

Model 2	WBES		PICS	
	Tax Evasion	Bribery	Tax Evasion	Bribery
Firm Level Variables				
Control Variable				
Firm Size	-0.29***	-0.05	-3.14***	-0.1**
Independent Variable				
Family-controlled Firms	0.11	0.08	1.36	0.34***
Interaction between Country Level Variables and Independent Variable				
Cultural Variables				
In-Group Collectivism* Family	0.04	0.12**	-0.98	0.19**
Power Distance* Family	0.13	-0.01	1.83*	0.16**
Social Institutions				
The Polity and Economy* Family	0.31**	-0.01	-0.31	-0.04
The Economy* Family	0.13	0.1	5.8**	-0.19**
Political Constraints* Family	-0.22	0.06	2.8	-0.11*
Control Variable				
Gross National Income Per Capital* Family	-0.23	-0.07	1.16	0.14

WBES Level 1: n = 3,731    PICS Level 1: n = 14,041

Level 2: n = 29

Level 2: n = 19

\* P ≤ 0.1    \*\* P ≤ 0.05    \*\*\* P ≤ 0.01

**Table 16**

HLM for Foreign-controlled Firms – Model 2

Model 2	PICS	
Firm Level Variables	Tax Evasion	Bribery
Control Variable		
Firm Size	-3.33***	-0.16**
Independent Variable		
Foreign-controlled Firms	-2.41**	-0.06
Interaction between Country Level Variables and Independent Variable		
Social Institutions		
The Polity and Economy* Foreign	0.96	-0.03
The Economy* Foreign	-1.4	0.1
Political Constraints* Foreign	-3.28***	0.47
Control Variable		
Gross National Income Per Capital* Foreign	0.59	-0.14

PICS Level 1: n = 14,041

Level 2: n = 19

\*  $P \leq 0.1$  \*\*  $P \leq 0.05$  \*\*\*  $P \leq 0.01$